

The Ukrainian Week

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Minister Volodymyr Demchyshyn
on energy, politics and oligarchs

Agriculture and rural
communities in Ukraine's economy

The background and influence
of the Right Sector

THE HARDER THE BATTLE, THE SWEETER THE VICTORY



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BRIEFING

Learning Independence

Anna Korbut

A 35 year-old woman pushes a wheelchair with a trim man of the same approximate age. He has lost both legs. The two are on their way to one of Kyiv's many parks, where a group of children is screaming, running and laughing—they come on weekends with their parents from the entire neighborhood. Not far from the park is the military hospital. The pair rolls up to a bench where other handicapped men are sitting. Some are missing arms, some with only one leg. A little boy stares at them and his parents explain that these men have come back from the war, that they were defending us against our enemy, Russia. »

In the middle of the night in a small town in Western Ukraine, a siren suddenly wails from the roadway as a column of cars drives along the sleepy highway and fades away into the silent night. When someone asks what's going on, they are told that a soldier's body is being taken from the front to his hometown to be buried. It's been like this for the last year and a half, although in the summer of 2014, such sirens were heard far more often. In the local town's social networks, these corteges are announced in advance, so people come out, line up along the highway with lit candles to say good bye to the soldiers on their last journey. Locals say it's good that his mother died when he was still little and his father passed away a year ago, because they won't experience the death of their son.

Some 10 years ago as a sixth grader, this boy stood on the weekly line-up that was the Monday-morning tradition at Ukrainian schools: the pupils gathered, sang the national anthem and, it would seem, read verses from a poet whose birthday happened to fall in that week. For most of the kids, this was a strange routine with a purpose they did not understand, something they went through just because. After school, the older pupils dreamed of running away to bigger cities, and, if possible, abroad. Not in order to travel around, see the world and learn something, but simply to leave a place where "nothing changes, and nothing happens." The teachers with their wretched salaries were busy thinking about how they could feed and clothe their families. Few of them felt inspired enough to explain to their pupils what they should appreciate and respect their anthem or statehood for. The poets whose verses they read and who, more than likely, spent a decade or more in the soviet Gulag for writing in their own language or even just criticizing the regime did a much better job of conveying this.

Now, this legless soldier is being sent money from strangers for treatment or for a wheelchair. Someone has organized courses where crippled veterans can learn IT or gain some other qualifications. At every bazaar, boxes stand where plastic lids are collected and melted into prostheses. The dead boy's classmates help his sister organize the funeral. One of them has been collecting and bringing care packages to the front for a long time now. One has been passing on humanitarian assistance to IDPs from the east. One of them studied at the Sorbonne and returned to work in Kyiv on a project whose goal is a liberalized visa regime with the EU. There are also many people who live ordinary lives, watch the news on TV from time to time, and worry what will be next—for mercantile reasons.

For all these people, August 24 is unlikely to be a holiday, at least not now. The war has died down, but it's far from over. No one understands in the least how elections will take place in occupied parts of Donbas, and what role the terrorists will play once they are amnestied after the elections. Will Ukraine continue to have to make concessions to calm down the aggressor? People are feeling angry that reforms are going slowly and those in power appear to be only taking superficial steps or doing things in response to pressure from civil society and the West. And this is in the heart of the capital, where a posting in

Facebook can get a decent sized rally complete with journalists and cameras happening outside the Prosecutor's Office within an hour. In those places where journalists and cameras never go, even less change is evident. Ordinary Ukrainians are worried about lay-offs, unemployment, and how they will pay for the new rates for gas and electricity. Few of them feel like celebrating.

Yet, those events that once seemed like empty officiousness barely transformed from soviet days are seen differently today. Now, independence and the attributes of an independent state such as the anthem or the flag are seen more as the right to fight with all of the problems listed above. To get there, Ukraine had to fight its own regime on the Maidan and then the remnants of the old system who are only willing to change under the rod, but even more so with the big neighbor. Fear of confrontation with Russia left both Ukraine and Georgia denied even the prospect of protection by NATO's wealthy, developed countries. Ukrainians know very well what will happen if they lose this battle, which is why, when western observers start to say "if Ukraine survives," most Ukrainians would prefer to leave out this particular "if." Young Ukrainians in particular, who have been disillusioned by the West's failure to defend its values, understand that no one needs them abroad and that their efforts and determination work are needed—and work—at home.

These days, you also hear the phrase "Nothing's changing" an awful lot less. Understanding has emerged that to see change, we shouldn't wait for



NOW, INDEPENDENCE AND THE ATTRIBUTES OF AN INDEPENDENT STATE SUCH AS THE ANTHEM OR THE FLAG ARE SEEN MORE AS THE RIGHT TO FIGHT WITH PROBLEMS

someone else to bring it about, that without our own efforts, they won't happen. That's why so many volunteers drive to the East, work on drafting reforms, help refugees settle into a new place, and buy medications for the wounded. That's why local activists let journalists know about huge illegal diggings for amber, despite the threat of potential and often actual physical payback from criminal elements and representatives of the old "law enforcement" system who provide cover for business and put a fair penny into their pockets as a result. That's why volunteers organize trips for children of veterans of the ATO or IDPs to vacation in the Carpathians. That's why many, although not all, Ukrainians are trying to do something, however small, for the overall goal.

This goal, the possibility of change, and the opportunity to make that change stick brings meaning to the idea of independence for many ordinary Ukrainians today. It has become something that is not officious and abstract, but something absolutely attainable, complicated and still distant, yet something that gives them drive. The crippled veterans and the lit candles that trail several kilometers down the sidewalk after the funeral of yet another fighter make sure no one forgets the price that this Day has cost us now. ■

Truth Out of Fashion

Edward Lucas

My copy of “Harvest of Sorrow”, inscribed with some kind remarks by the author, is one of my most treasured possessions. Robert Conquest, who died this week aged 98, was one of the great truth-tellers of the past century. He unearthed in unprecedented detail the story of Stalin’s mass murders — the artificial famine in Ukraine, the human meat-grinder of the Gulag, and the destruction of whole nations in the maw of the Soviet empire — at a time when much bien-pensant opinion in the West preferred fair-mindedness over clear-sightedness.

They still do. Truth is out of fashion in many quarters, along with the idea that terms such as right and wrong have a meaning. One reason for this is intellectual fashion, which highlights subjective interpretation over objective reality. Instead of a single truth, we have multiple narratives. Who is to say whose narrative is better? It is much easier to take this approach than to accept that one side is right and the other wrong, and then to think about your own moral responsibility for what you do.

In some circumstances this is sensible. Modern literary criticism rightly encourages us to think that the same text may mean different things to different readers. You can read George Orwell’s 1984 and interpret it as a story mainly about love, or about dictatorship, or about memory. Neither version excludes the validity of the other. But this approach has its limits. When Winston Smith insists that O’Brien is holding up four fingers not five, he is telling the truth. Any other answer — no matter how much conviction is behind it — is a lie.

In the same way, blame for the downing over Ukraine a year ago of the Malaysian airliner MH17 can land in only one place. Either Russian-backed rebels shot it down, in which case responsibility for mass murder lies with the commander in chief, Vladimir Putin. Or (as Russians claim) the Ukrainians did, in which case the blame lies with them. Despite Kremlin propaganda efforts to muddy the water, all the evidence points to Russian rebels as the culprits. Yet the media still present the two versions of events as comparable. One can imagine the modern BBC reporting, with studious fairness, that: “Mr Smith asserts that only four fingers are on display whereas Mr. O’Brien maintains there number is five.”

Conquest, along with Orwell, worked for a while in a (now-closed) information-warfare division of Britain’s Foreign Office. Both men understood how powerful a weapon lies can be, especially when backed by fear. The lies can be blatant or subtle. But either way they



corrode decision-making and distort public opinion. Correcting them is tedious and expensive.

In those days there was little dispute about who should pay for such work. Western taxpayers financed the information war against Communism in the same spirit that they had paid for (or in the case of some occupied countries listened to) anti-Nazi broadcasts during the war.

But since the collapse of Communism, Western countries have gutted their public information services. They are only now beginning to pick up the pieces. Britain has a new military unit devoted to psychological warfare and social media. The Foreign Office and the State Department have produced some sharp material rebutting the more absurd Russian claims about the West and its allies. But the best efforts are closer to the frontline — such as the estimable StopFake in Ukraine.

Ukrainians make huge efforts, despite dismally disappointing political leadership and scant resources, because they can imagine what their coun-

IT IS MUCH EASIER TO TAKE THE APPROACH OF MULTIPLE NARRATIVES THAN TO ACCEPT THAT ONE SIDE IS RIGHT AND THE OTHER WRONG

try will be like if they lose. Most Westerners cannot make that leap of imagination. The crackdown on human-rights lawyers in China, or squabbles about reefs and rocks in the South China sea, have little bearing on daily life. Nor (for many Westerners) does Russia’s war in Ukraine, or the menacing of its Nordic and Baltic neighbours. The migration crisis and the plight of Yazidi sex slaves in ISIS captivity are distressing, but we can still turn the page on them. It is easier to nit-pick at our own shortcomings than to fret about far away problems.

That is the approach taken by the followers of Edward Snowden, Noam Chomsky, Glenn Greenwald — and now Jeremy Corbyn. Rather than wrestle with the real questions of how to deal with authoritarian crony capitalism in China, or Russia’s aggression in Ukraine, or the rise of murderous Islamism, they turn their inwards to the faults of the West, be they snooping by the NSA and GCHQ, or wider woes such as militarism, corruption, abuse of power and hypocrisy.

Some of these problems are real, others imagined. But it is the hallmark of a free society that we can discuss them and try to fix them. People living under dictatorships cannot. Orwell and Conquest understood — and defended — that difference. So should we. ■

Cloning Saakashvili

Denys Kazanskyi

Proposed decentralization raises concern over the quality of human resources available to run the regions

After the widely announced extension of powers for local governments, mayors, councils, heads of state administrations and other regional officials, that follows the administrative reform, they will have to work harder and make more responsible decisions than they do now. Will the people working today in executive committees and regional administrations be up to this task?

Given the current situation anywhere beyond the central government in Ukraine, this seems highly unlikely. While top central authorities that constantly find themselves in the spotlight of the media and foreign politicians and experts are doing some personnel purges, and even show some progress, the regions see stag-

nation in that. Newsworthy appointments and lustration of civil servants in the regions are sporadic. Most often, local officials who have long been embedded into the corrupt state machine and who, during the years of service, developed an amazing ability to survive under any government, remain in office.

The work of the Cabinet of Ministers and the staff of the General Prosecutor's Office is closely scrutinized by the journalists. The media provide regular updates on the raids by Deputy Prosecutor General Davit Sakvarelidze on corrupt prosecutors, as well as on the work of the new police force created under the management of First Deputy Minister of Interior Eka Zguladze. Georgian and Lithuanian top officials have



Heorhy Tuka, the first volunteer to head an oblast state administration.

He replaced Hennady Moskal as the Head of Luhansk civil-military administration on July 22

noticeably animated Ukraine's political scene, and news stories featuring them encourage us to believe that reforms in Ukraine are underway. But what do we know about the work of local authorities in the regions, those responsible for implementing the decrees and orders issued by the ministers in Kyiv?

The main non-Kyiv newsmaker is Mikheil Saakashvili, the newly-appointed Head of Odesa Oblast State Administration. In about two months since his appointment in late May, he has managed to create so many newsworthy events that other heads of regions would hardly do in a year. In late July, Maria Gaidar, the daughter of Yegor Gaidar, the father of Russian privatization, joined his team, instantly becoming the most talked-about Ukrainian Deputy Governor ever.

Beyond Odesa Oblast, however, opposite trends are more common. Of particular concern is South-Eastern Ukraine.

In April, Yehor Firsov, a Donetsk-born Bloc of Petro Poroshenko MP, wrote in his blog that the President's team appoints former members of the Party of Regions as heads of county administrations there, instead of looking for new young staff.

"The Presidential Administration relies on the 'team of professionals' nurtured by Liovochkin and Kliuyev'. For what I know, the Bloc of Petro Poroshenko didn't even try to consult any of my colleagues in the Parliament on personnel issues. For example, UDAR group within the BPP faction, of which I am a member, is hardly represented in the presidential power structure. Given the fact that Deputy Chief of Staff Vitaliy Kovalchuk comes from our party, he should know better than anyone else the talent pool of our regional party structures.

The conclusion is unnerving: one of the major issues of public administration—staffing—remains unresolved. The appointment of officials was and remains obscure. The major condition for getting a job at an oblast or county state administration was and remains loyalty. The system offers no social mobility, and people who have not been in government will never get into it," Firsov wrote.

To prove his words, he quoted a list of county state administration heads in Dnipropetrovsk Oblast: 17 out of 22 counties are headed by former Party of Regions people.

This gives us a puzzling general picture. While President Poroshenko appointed an experienced and media-friendly reformer to Odesa Oblast, in Dnipropetrovsk he preserved the old staff that served as the backbone of the corrupt regime for years. Such personnel policy can hardly signal any intent of serious reforms in the region.

The heads of oblast administrations raise many concerns too. Anyone who watches the public flogging of corrupt officials or personal supervision of the demolishing of an illegal fence on the city beach by Odesa Governor Mikheil Saakashvili, starts wondering why he is the only one out of the 25 heads of oblast administrations to act this way? What prevents others from demolishing illegal constructions or thrashing corrupt officials? What stopped Zhytomyr Governor Serhiy Mashkovsky from going to illegal amber extraction fields and admonishing the corrupt local police and prosecutors?

All this points at an obvious conclusion: if the heads of oblast and county administrations are reluctant to work the way Saakashvili does, they should be dismissed. After all, we already have a model regional leader who finds ways when there is will. But Ukraine cannot have Georgians as heads of all of its regions. We need local talents to entrust the regions, since it is regional leaders who will in the future have more power than they have today. It is also worth remembering that weak and indecisive leaders of Donetsk and Luhansk oblast state administrations contributed to the ignominious surrender of the places to the Russia-backed militants. In Dnepropetrovsk, to the contrary, an influential leader quickly had separatists over a barrel.

Clearly, to achieve progress in reforms, we need people from outside of the system to take the posts of oblast governors. The regions need people who are not part of the chain of corruption, but have administrative experience. Saakashvili may be well-tailored for this position, but Ukraine abounds in proper professionals as well.

The best foundry of future management talents is the volunteer community. Volunteers are good organizers and enthusiasts, as well as dedicated patriots, which, given the resilience of the corrupt state machine, is probably the most important criterion. It looks like the higher-ups have realized that such path

TO ACHIEVE PROGRESS IN REFORMS, WE NEED PEOPLE FROM OUTSIDE OF THE SYSTEM TO TAKE LEADING POSTS IN THE REGIONS

is inevitable. As a result, volunteer Heorhy Tuka was appointed Head of the Luhansk Oblast State Administration. Ideally, this appointment should be followed by more of the kind.

It is the volunteer community that established over the last year its own ministry of defense, which often works more efficiently than the Ministry headed by Stepan Poltorak. People who, without asking permission and without much ado, took over the functions of the state and performed them without asking for awards are definitely more worthy of holding a public office than the thievish turncoat officials.

Another important talent pool are businesspeople. The only thing is that in order for the former and the latter not to get mired in the corruption swamp, the new officials need to earn an adequate salary. With the current award offered to civil servants, only people who can rely on their savings can take the job.

Without an HR revolution in the regions, there will be no one available to bring to life ambitious and urgent initiatives of the President and the Prime Minister. Old functionaries will inevitably fail any revolutionary endeavors and innovative approaches. We have no room for such mistake. ■

¹ Serhiy Liovochkin served as Chief of Staff under Yanukovych from February 25, 2010 to November 30, 2013, filing resignation letter over disagreement with actions against Maidan protesters. Andriy Kliuyev served in various top positions in the Yanukovych government, including as Vice Premier and First Vice Premier, head of the National Security and Defense Council and Chief of Staff for Yanukovych from January 24 through February 25, 2014. He fled Ukraine in early June 2015, after the Prosecutor General's Office put him on the wanted list for suspicion of abuse of public power and fraud.

Volodymyr Demchyshyn:

“Things aren’t critical in the energy sector. It’s just highly politicized”

Interviewed
by
**Tetiana
Omelchenko**

Ukkraine’s Minister for the Power and Coal Industries talks about the gas balance, the chances of modernizing this sector, and the role of oligarchs in the Fuel & Energy Complex in an exclusive interview for *The Ukrainian Week*.

Today, Ukraine’s gas storage system contains 1.8bn cu m less natural gas than it did one year ago. Thanks to a warm winter, Ukraine was able to get through the last heating season more-or-less without losses. What factors might ensure an equally normal heating season this year, if the winter happens to be cold?

Comparing to last year is not an indicator. To understand how the heating season works and estimate how much gas will be needed, you have to look at a different indicator, consumption. And this depends both on how cold the winter is and on the economic activity and energy efficiency of consumers. Today, 40 million cu m are being consumed a day by residential and industrial users. In winter, this can go up to 200mn cu m/day and even 300mn cu m/day during severe cold spells. Based on the average winter, the math goes

like this: we use 200mn cu m/day, we extract 55mn cu m of our own every day, we can pump up to 60mn cu m/day through reverse flows, as long as there are funds for that—right now we’re only buying 30–40mn cu m/day. This means we need to use a maximum of 120mn cu m/day of the gas that’s in storage. In this case, we get through the winter without renewing deliveries from the Russian Federation.

But I’m pretty certain that the decision will be made to renew gas deliveries from Russia any day now. Last year, gas was coming in from Russia and we didn’t have to take the maximum quantities of fuel from storage every day. And so we didn’t need much in the way of reserves. On the other hand, 2bn cu m were supplied to the occupied territories and no one paid for them. So the fact that there’s 1.8bn cu m less gas in the underground gas storage system (UGS) this year is not a problem. We can fill it up in 15 days if the money’s there.

What alternatives are there?

Well, if Russia offers us a decent price and guaranteed deliveries, then we will be getting gas from three different sources at the same time: reserves (60mn cu m/day) and RF gas (114mn cu m/day is the maximum that we can buy from them), plus 55mn cu m of our own gas. If this happens, we will cover all our demand and won’t have to dip into the UGS at all. Ukraine has a huge UGS system. It can handle super large volumes from both Russia and Europe and pump major volumes in and out of the UGS on a daily basis. We can do fine with any of the alternative, with one caveat. If the winter turns out to be really cold, we will need the flow from Russia. We can survive the winter without Russian gas, but only if the temperatures aren’t extreme. If there is a serious



chill, it won't matter what we have in storage, even if there's 30bn cu m there. When the temperature drops really low, demand rises to such a point that we can't get the gas out of the storage tanks fast enough.

You said that plans are to have 19bn cu m in the UGS before the heating season starts. Experts say they don't see this happening without deliveries from Russia.

That's true. Without Russian deliveries, it won't be possible to put away 19bn cu m. But prior to this, I talked about daily consumption to demonstrate one point—that there's no force-majeure situation with supplies right now. This sense of force-majeure is being blown out of proportion in order to spur Ukraine to accept Russia's conditions and buy gas at US \$247.17 per 1,000 cu m. We refuse to do this on principle, not just because of the price, but also because of Russia's rigid stance. Firstly, it refuses to set a price for the entire heating season and to sign a three-way contract with the participation of the EU. For us, this is extremely important: we not only need a low price, but also guarantees that the price won't change for the entire heating season. Otherwise, we could find ourselves without a contract in the middle of the winter and that would be a serious problem.

But I'm confident that we will reach an agreement: we buy Russia's nuclear rods, coal and power from Russia. We need to develop normal commercial relations, despite the war. We have no choice. Otherwise, we'll have to cut power and heating. If, in the end, there won't be any deliveries of Russian gas, we'll have to start looking at a force-majeure situation. That's where the 19bn cu m figure comes from, that's what we need. Right now, we have 13.2bn cu m of natural gas in the UGS.

How prepared is Ukraine to pay for the missing volume of gas?

Theoretically, we can pump 4.8bn cu m without Russia for US \$255, as that's what reverse-flow gas is costing us. This is US \$1.2bn and it's money that we don't have right now. We are looking to cover at least 63 days in advance. Every day, we're pumping in 75mn cu m at US \$255 because we can't afford any more than that. That works out to US \$18.8mn a day.

What happened that Ukraine refused to pump imported gas from Europe during the first half of 2015, when Russian gas was being delivered? Surely you were aware of the risk that Russia might stop sending gas our way at any time.

This was not a particular position. All we were concerned with was getting gas at the lowest possible price. At some points, Russian prices were cheaper than European ones and Naftogaz has been doing everything to buy gas at the cheapest available price. Incidentally, European gas prices go down the minute Ukraine stops taking deliveries, so sometimes it's better that we buy less in Europe so that the price stabilizes.

What steps is the government taking to increase domestic extraction?

We raised the price for Ukrgezvydobuvannya, the main extracting company, by 70%. For it to do a better job, money has to be invested in drilling equip-

ment, exploration work, and upgrading infrastructure, because our deposits are old. And everything is limited by the budget, of course. In order to extract more gas, we need investment capital. Some capital can be gained by increasing the price, using budget revenues, or finding investors. Needless to say, investors won't come to a country at war. The budget is empty, with all its resources going to social needs and defense. The only option is to raise the price for Ukrgezvydobuvannya. Taking a small amount of money, repairing the old wells and increasing extraction is less costly than drilling new wells. And that's what we're doing now.

Private drilling companies have seen their leasing costs go from 28% to 55% of extraction value for wells up to 5 km deep, which is most of the wells in Ukraine. These companies also pay the VAT and other taxes. The top seven Ukrainian companies in Ukraine extract a total of 3.5bn cu m annually and these terms are not convenient for them. The risk is that they will stop extracting and exploring altogether because they are not making any profits. We've been proposing them lower rates to give them incentive to extract and offset general revenues. We persuaded the Finance Ministry that the optimal rate is 29%. We also need to streamline the procedure for issuing permits. Right

THE SENSE OF FORCE-MAJEURE IS BEING BLOWN OUT OF PROPORTION IN ORDER TO SPUR UKRAINE TO ACCEPT RUSSIA'S CONDITIONS AND BUY GAS AT US \$247.17 PER 1,000 CU M

now, you need more than 80 permits at various levels of government just to commission a well. We've reviewed the list and plan to cut it considerably and institute timeframes for issuing the documents.

What kind of numbers does the Government have to show the results of energy conservation measures this past year, in terms of reduced consumption levels?

Most of the savings have come from industrial users, who have reduced consumption and become more energy efficient. Consumption went down 2bn cu m in the last period, which is worth US \$500mn. Firtash's companies have begun producing fewer farm chemicals, the Odesa Port Plan is using less ammonia, and some furnaces are being switched from gas to hard fuel. Everybody is trying to cut down consumption and this is the result of equalizing rates.

Deputy PM Voshchevskiy has said that you could be dismissed in the fall. When the miners came to Kyiv and launched huge protest rallies, they were demanding your resignation because they aren't being paid and the coal industry isn't being reformed at all. Premier Yatseniuk has also publicly expressed dissatisfaction with your work and referred to the situation in the fuel and energy complex as "critical." How long do you think you will hang on in this position?

The situation is not critical in the energy sector. There's just a lot of criticism, politicking and private interests around it. Things are "bad" in the sector because I have a strong position against the monop-

olists, who are lobbying their interests at a certain level. For years, key positions in the Ministry were like a petting zoo that simply protected certain financial interests. I brought nearly 35 independent specialists who managed to stabilize the situation with the heating season within 20 days and to put an end to rolling blackouts. What's more, this team paid no attention to those who were covering—and in places are still covering—various corrupt schemes.

Of course, nobody is happy about this, so in public, Demchyshyn is the bad guy. My job is to be a lightning rod so that my team can do their job. If my position were taken by the protégé of some populist politician, he'd already have been awarded a heroic order. We could have all had a chestful of medals if we had just raised the rate from UAH 0.80/cu m to UAH 1.20/cu m, which is what DTEK, the monopolist on the cogeneration market [Rinat Akhmetov's company], wanted us to do. People would be paying even higher rates now and the press would be calling me the best minister ever. DTEK spends US \$10mn a year on PR for good reason. All I can do is remind the Government, every two weeks, that DTEK still owes the state UAH 400mn for coal deliveries and that's why the Ministry is unable to pay miners their wage arrears. But no one is paying attention to any of this.

How would you assess the situation in the energy sector?

The energy sector is a key segment of the domestic economy, providing 30% of GDP, yet people have been robbing it for the last 20 years, because it has a constant cash flow thanks to people paying for electricity every day. But instead of developing, the market is stagnant, money is not being invested but wasted—either in poorly managed state-owned enterprises or in the accounting machinations of private companies. For instance, DTEK miners are standing outside our walls begging us to raise the price of coal and electricity rates. Nobody has bothered to remind them that, after the last increase in 2014, their salaries actually fell 5%, rather than being raised, because their wages depend on a private owner who spends the money coming in from the power stations and mines he owns, not on salaries but on private planes, property and the acquisition of more oil and gas enterprises. If the state does raise electricity rates, all of us will simply be paying Rinat Akhmetov's debts back for him.

Why? Because no one has been putting anything into modernizing in the past few years, only into acquiring new assets. His management has come to me for help in covering a US \$3bn debt that is owed to creditors. But they can't explain where all the money went. If we were just allocated UAH 1 billion—which is not a lot of money for the state—, to modernize the equipment in our mines, they could be operating in the black within half a year. We'd have both coal and wages for miners and the need to take money out of public coffers would disappear. Today, these mines are costing the state UAH 250mn a month. Wages need to be paid, equipment's outdated and worn, and there goes the economy...

Will the government actually give you UAH 1 billion to modernize?

Volodymyr Demchyshyn was born in 1974 in Lviv. He graduated with a degree in international relations from Ivan Franko National University in Lviv and received an MBA in international finance from the University of Kansas Business School in the US. Demchyshyn was director of Investment and Banking Services at Investment Capital Ukraine. Prior to ICU, he was vice-president of ING Bank, and Corporate Finance manager with Ernst&Young. From August to December 2004, he chaired the National Electricity and Residential Services Regulatory Commission. Since December 2014, Demchyshyn has been Minister of the Energy and Coal Industry.

The Cabinet of Ministers keeps stating that there's no money. As I've explained, this is a game with only one net: state mines need to be competitive. Otherwise DTEK, as a monopolist, will dictate all the rules of the game unilaterally. All the coal that Ukraine needs can easily be supplied from this company's mines. Once it squeezes the state out as a market player, DTEK will be able to dictate the "production cost" and set rates as it wishes. There won't be any competition. And so, I keep trying to persuade my colleagues that this situation needs to be broken once and for all, regardless of the arsenal of pressure being placed, from paid-off deputies to the paid-off press.

In other words, you have no intention of quitting, come fall.

I have plenty of issues that need working on every single day in order to maintain the situation and not lose the energy to implement reforms. Of course, the Verkhovna Rada could vote to dismiss me, but I will not resign of my own accord. That's not what I've been digging to clear this mess up for, for the last six months. I won't give up so easily.

How likely is it that the miners will strike again? How easily can the oligarchs—specifically Rinat Akhmetov—manipulate them?

IF PEOPLE ARE PREPARED TO COME TO KYIV, SLEEP IN A BUS AND YELL WHATEVER SOMEONE TELLS THEM TO YELL ALL DAY LONG FOR UAH 500, THEN STRIKES ARE POSSIBLE

If people are prepared to come to Kyiv, sleep in a bus and yell whatever someone tells them to yell all day long for UAH 500, then yes, it's possible. To make miners' lives safer, money has to be spent. Over the last half-year, the state hasn't allocated a single kopiyyka to the mines so that they can develop. It's barely paying out wages.

But you're not saying anything about Akhmetov's own role in possible future strikes...

Let's hope that during the previous series of campaigns he understood how little benefit they brought him. And they cost him a pretty penny: a minimum of UAH 30mn.

What can you say about the state of Ukrtransnafta, the state oil transport company?

¹ Kolomoyskiy's bank and the biggest in Ukraine.

Ukrtransnafta is a 10% state-owned corporation that issued UAH 409mn in dividends in the last three months, it opened its books to investors, it cut costs and it ended up with an estimated more than UAH 1.5bn in profits. What's more, we raised the fees for transporting petroleum, so there are some positive results for the state. We've been slowly changing the management: the board of directors and key regional representatives in Kremenchuk, Brody, Kherson and Odesa. In short, the company is under state control again and it's in the black. Ukrtransnafta has nearly UAH 2bn on deposit with PrivatBank that will only become available in April 2016, which is clearly a bit of a problem. We sometimes hear threats from the company's former president, Oleksandr Lazorko, who signed the contract to store technological petroleum for a year at a 0 rate and then changed his mind and signed it at a rate of UAH 6 per tonne per day. This alone already amounts to more than UAH 650mn. In short, Lazorko has caused the country considerable losses and I'm not sure why there hasn't been an investigation so far.

What about Ukrnafta? Has Ihor Kolomoyskiy's resistance been overcome?

Here, the situation is a lot more difficult because ownership is nearly 50/50. Because there's no love lost for Kolomoyskiy in certain quarters, there have been calls to take away his ownership rights to the company. But we're supposed to be building a democratic country, and he owns 50% of the company, which he acquired on the open market. I'm often accused of "cooperating" with Kolomoyskiy simply because I state the facts, but I simply favor solving problems using professional methods, not going to war.

Kolomoyskiy has legitimate beefs against us: the government used some of his gas and never replaced it. We, on the other hand, have the opposite complaint: he hasn't been paying any fees and we suspect that the volume of extracted gas that was published is underestimated—which means that not all the company's profits are transparent. In addition, some of the natural gas that was supposed to go to Naftogaz Ukrainy was refined at Kolomoyskiy's Azot plant instead. And finally, he reported that last year UAH 2bn was spent on geological exploration, but then told the market that no such work ever took place... All these issues have to be carefully investigated.

How much more effective will this new management be?

I should hope it is. If it turns out not to be any better, it will have to be replaced. Its first task is to do a thorough audit of the company's activities over the last two-three years and to determine the situation with dividends, profits and liabilities. I'm confident that, in time, Ukrnafta will pay taxes, rent and VAT. Right now, the law is being changed and the Supervisory Board, which includes six individuals representing state interests, has the opportunity to make binding decisions. This is a serious instrument for influencing the minority shareholder. Mr. Kolomoyskiy understands that and I expect him to meet us half-way. ■



The Power of Rural Ukraine

Oleksandr Kramar

Consolidation of villages around towns will accumulate up to a half of Ukraine's population in agricultural communities and encourage them to actively participate in sociopolitical life

Ukraine is widely perceived as a predominantly urban country, with the rural population constituting a minority that lives in socioeconomic backwater on subsidies from the state. In the pre-Maidan Ukraine, the share of urban population was 69%, going down to 68% after the occupation of Crimea and parts of Donetsk and Luhansk oblasts. However, reality is very different from official statistics and reveals a more complex problem.

By the share of agriculture in GDP, the structure of employment (**see Coming Back to Earth on p....**), or the share of people living in rural areas, Ukraine is increasingly becoming an agrarian country. On the one hand, this signals that Ukraine's prospects depend more than we believe on solving infrastructural, social and economic problems in agriculture-focused areas. On the other hand, this proves that doing so in the traditional paternalistic way, when villages and agriculture were subsidized by cities and urban industry as in the Soviet Union, or as in rich Western countries with an insignificant share of agriculture and low density of population in agricultural areas, is impossible.

Solving the problems of agricultural areas should be primarily the project of their residents financed from their own resources. The role of the central government there should be reduced to creating conditions that would stimulate and facilitate it. The success, however, will depend entirely on the ability of the residents to become more active socially and politically. This would contrast with their long-lasting traditional hibernation and exceeded expectations placed on regional and national governments to address all local problems.

SPECIFICS OF URBAN UKRAINE

Though the share of overall urban population in Ukraine has not changed officially in the recent years, there have been significant shifts between the shares of population in cities and towns of different sizes. Out of 52 Ukrainian cities with over 100,000 citizens as of 2014, 15 are in the territories occupied by Russia (6 in Crimea and 9 in parts of Donbas). These include 5 out of 13 cities with 300,000 to 1,000,000 residents. In the rest of the Ukrainian territory, the share of residents in major cities with the population exceeding 1 million (Kyiv, Kharkiv, and Odesa) has grown. So has the share of people living in towns with populations of 20,000–25,000.

Estimates based on the current official statistics from the central and regional statistics bureaus

show that, as of the early May 2015, the actual population of Ukraine (excluding the occupied territories) counted 39 million. This figure did not include IDPs from the occupied parts of Donbas since their number is impossible to determine precisely at the moment.

Out of these 39 million, 26.6 million officially qualify as city residents, and 12.4 million as the rural population. However, only 18.2 million of the urban population live in cities with over 50,000 residents (settlements below this mark qualify as towns). The shares of such urban population are very uneven throughout Ukraine: unlike the handful of compact hubs where urban population is concentrated more heavily, in other parts of the country its share is fairly low, ranging anywhere between 20 and 30%.

The population of these compact hubs totals 10 million. They include the "Greater Kyiv" that covers Kyiv, Brovary and Irpin and is home to 3.08 million residents; Prydniprovsky region including Dnipropetrovsk Oblast and the adjacent Zaporizhzhya and Zaporizhzhya district with 3 million; Kharkiv with 1.45 million; the "Greater Odesa" covering Odesa and Illichivsk with 1.1 million, and the Ukraine-controlled part of Donetsk Oblast with 1.4 million people.

Beyond these hubs, the share of city residents (meaning cities with over 50,000 people) is a little over 28.3%. In most oblasts, this population is concentrated in oblast capitals (Vinnytsya, Ternopil, Chernivtsi and Rivne oblasts) and a couple more



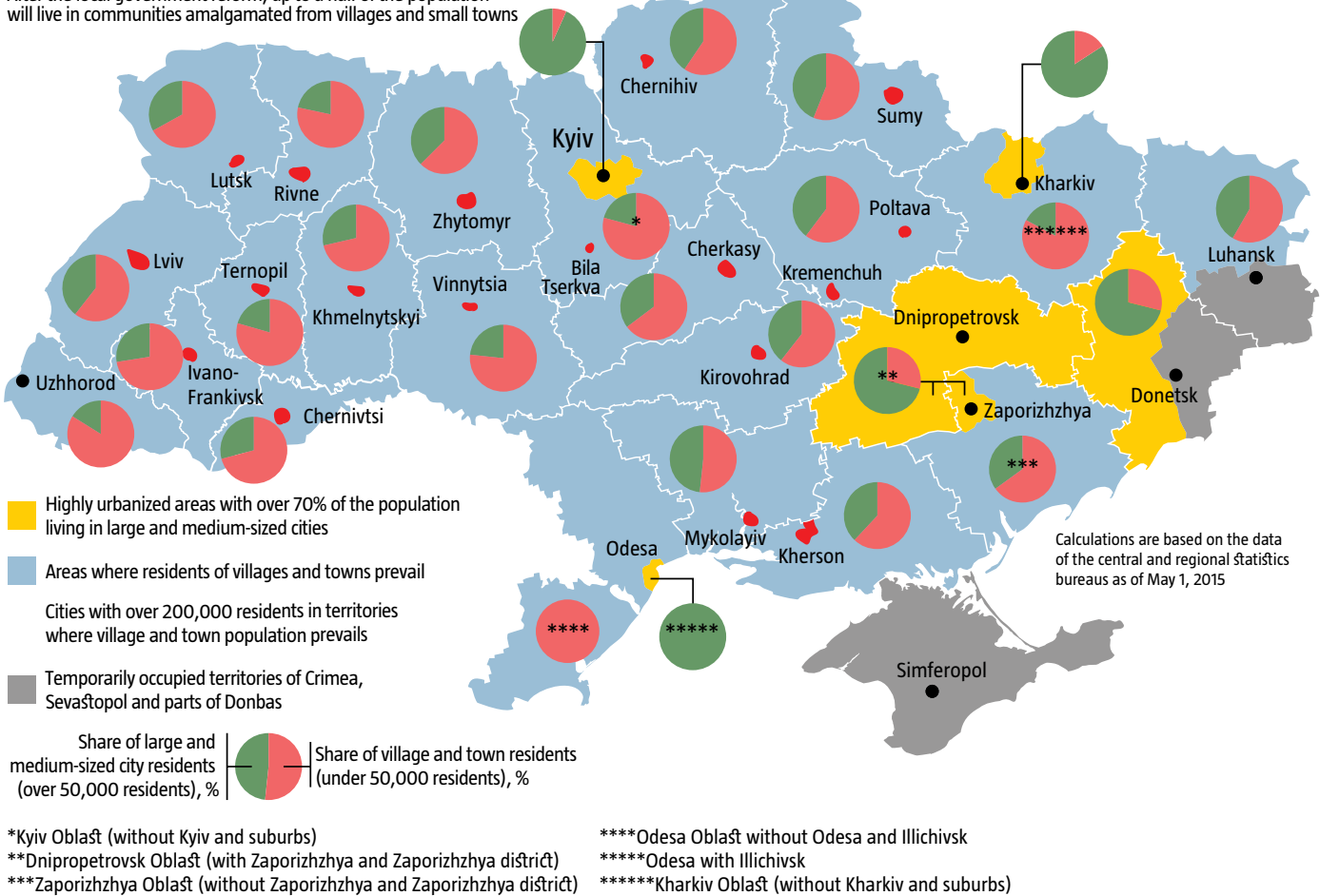
SOLVING THE PROBLEMS OF AGRICULTURAL AREAS SHOULD BE PRIMARILY THE PROJECT OF THEIR RESIDENTS FINANCED FROM THEIR OWN RESOURCES

cities with populations of 50,000–100,000 in Zakarpatska, Khmelnytskyi, Volyn, Zhytomyr, Poltava, Ivano-Frankivsk, Kirovohrad, Mykolayiv and Kheron oblasts.

Overall, with the abovementioned hubs excluded, urban population is distributed fairly evenly in the West (28.3%), South (30.9%), Center (33.1%) and East. For example, 27.5% of the population in the Ukraine-controlled part of Luhansk Oblast, live in cities with over 50,000 residents. The share for Zaporizhzhya Oblast and its suburbs adjacent to Dnipropetrovsk Oblast is 35%.

Small-town life

After the local government reform, up to a half of the population will live in communities amalgamated from villages and small towns



Thus, in most of Ukraine's oblasts residents of towns with less than 50,000 populations prevail. This often distorts sociological surveys carried out by companies which focus on large cities only, even though the sentiments of residents in smaller cities in Central and Western Ukraine differ significantly from those in their oblast capitals, let alone in large and medium-sized cities concentrated in the above five hubs.

TOWNS AND DECENTRALIZATION

67 of Ukrainian towns have over 20,000 residents rely on non-agricultural sectors: Ladyzhyn, Enerhodar, Netishyn and Slavutych have a well-developed energy industry; Fastiv, Kozyatyn, Zhmerynka are major transportation hubs; Myrhorod and Truskavets are popular tourist destinations. They have the total of around 2.1 million residents. The remaining 6.3 million urban residents live in standard small towns.

Back in the Soviet times, most towns had one or even two large agricultural enterprises (collective or state farms) with at least 1,000–1,500 employees. After the land reform, the employees were given land allotments that are either rented out or cultivated independently by their families today. Like the rural population, most residents of these towns have pri-

vate housing and live off subsistence farming, while others earn their daily bread from farming businesses or agricultural firms established on the basis of former soviet collective farms (which often belong to agricultural holdings).

Over the past 20–25 years, however, most unsustainable local enterprises have gone out of business and towns have become increasingly similar to the large villages around them. In towns with a county center status, most jobs and gross regional product are generated by the state budget-funded public bodies and social infrastructure institutions (hospitals, cultural establishments, etc.). Today, these towns are in the best position to become centers of the newly-consolidated communities, a status that would enhance their agricultural profile and further ruralize the existing towns.

Such towns and villages today are home to over 18.7 million residents (48% of Ukraine's total population). Cities with over 50,000 residents are home to 18.2 million (46.7%) people. Another 2.1 million or 5.3% live in the 67 cities that are in the stage of transition from towns to medium-sized cities. The latter in their majority will also become community centers integrating the surrounding villages, but they will have less of an agrarian component.

Many Ukrainians perceive the consolidation of rural communities (resulting from the decentralization reform) as merger of several former village councils into one. In reality, based on the new Government-approved Methodology for Capacities of Territorial Communities, it is current county or oblast capitals that will mostly be eligible for the status of community centers. Currently, Ukraine (except for occupied territories) has about 900 small towns and urban settlements. After decentralization, about 1,200-1,400 communities have to be established.

The infrastructure of a potential community center, in addition to secondary schools, polyclinics/outpatient departments, preschool and afterschool facilities, must include premises suitable for public and law enforcement agencies, as well as offices carrying out civil status and property titles registration, pension provision, social security, fire safety, and treasury services. According to the "accessibility criterion", community centers must be no farther than 20-25 km in paved roads from the most remote community settlement. This is comparable with the distance from the majority of current county centers to the most remote villages in the county.

According to the information obtained from the regions, at least in Central and Southern Ukraine where old administrative counties with small populations (15,000-35,000) prevail, there is a strongly marked trend to form communities based primarily on the existing counties. Splitting a county into two or more communities will most probably become an exception rather than a rule. This could be a case either in the counties with populations of or over 50,000 and/or having within them at least two or three towns or urban settlements, or in rather large counties with low population density, primarily in the steppe and forest areas, where establishing communities basing on old county structure would mean exceeding the prescribed distance to the center.

The attempts of local village heads in some counties to form small communities (five to seven in small counties) by combining only a few existing village councils are at odds with the government methodology and, not least, with the interests of the old county administrations, which could retain and even consolidate their authority over the territories they previously controlled if their county centers become the capitals of the newly-amalgamated communities. Therefore, any attempts to set up numerous smaller communities within existing counties are likely to eventually be stifled by the lack of public funding.

CHALLENGES AND OPPORTUNITIES

The growing share of agricultural communities in population structure and the increased size of those communities resulting from the merger of villages will bring about both new challenges and new opportunities for their residents.

On the one hand, there is a risk that large agricultural holdings and large local landowners will establish control over communities and *povits*, groups of communities. This can lead to the degradation of infrastructure and growing rightlessness of local residents that could be far worse than under the rule of oligarchs on the nationwide scale. If con-

trolled by large landowners, local deputies, elected authorities and heads of executive committees, police and other bodies can bring life in rural communities much closer to feudal standards than it has ever been before. The *prefect*, an authority appointed by the central government and independent of local landowners, will also be very close (most today's counties will only have three or four *povits*) and have powers as wide as those of the present-day state administrations.

Another important aspect is that the residents of consolidated agricultural communities will gain importance as a powerful electoral resource in national and regional elections. They constitute a strong majority in most regions and provide at least half of the votes at the national level. Previously, they were traditionally used by public officials through administrative leverage. Now, especially with the growing weight of the agricultural sector and the holdings dominating it in Ukraine's overall economy, the owners of these holdings may soon try to privatize their constituencies and, quite possibly, even create one or more agricultural political parties.

On the other hand, consolidation will boost small businesses within each community and *povit* (farmers, owners of small food and timber processing facilities, trade businesses, transportation and service providers). There will be at least hundreds of them in the new communities, and thousands in regions—the post-decentralization version of the current oblasts. This will provide comfortable environment for the growth of effective local economic



CONSOLIDATED COMMUNITIES WILL BOOST SMALL BUSINESSES AND ENCOURAGE THEIR OWNERS TO COMPETE FOR POWER WITH LARGE LANDOWNERS AND AGRIHOLDINGS

and socio-political associations to promote their interests, solve pressing issues and exercise pressure on local authorities whom the community life will increasingly depend on.

In particular, the alliance of communities may give a new impetus to farmers' movement, who are primarily interested in countering the domination of agricultural holdings and landowners. This potential is particularly strong in regions with a developed farming sector. For example, Odesa Oblast has 5,200 farming enterprises, Mykolayiv Oblast has 3,900, Dnipropetrovsk Oblast has 3,300, Kirovohrad Oblast - 2,600, Kherson Oblast - 2,400, Zaporizhzhya Oblast - 2,300, Vinnytsya Oblast - 1,900, Poltava Oblast - 1,800, Zakarpattia Oblast - 1,500, Khmelnytskyi and Kyiv oblasts - 1,400, and Cherkasy Oblast has 1,300. This means that at least in these regions, each newly established *povit* will have at least 400-600 farms, and each community at least 50-100 of them. Such a development is especially likely if the local self-employed household farmers and entrepreneurs operating in adjacent branches of agribusiness find a common interest: their number in the communities will be at least 10-20 times higher than the number of farmers. ■



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Back on the Ground

Oleksandr Kramar

Agribusiness becomes the biggest component of Ukraine's economy. What will it take for the growth to continue?

Over the last decade, the structure of the Ukrainian economy has changed. Its Soviet legacy manifested in energy-hungry steel industry that is disconnected from the domestic market and uncompetitive globally, as well as most machine-building and chemical plants, is in decline, its output and employment shrinking. Agriculture and related industries (primarily food industry) have taken over. The trends discussed below refer to the production industry. Like in most other countries, non-production sectors (trade, services) have been growing in Ukraine.

In the pre-crisis year of 2007, the share of agriculture in Ukraine's GDP was a mere 6.6% while the processing industry accounted for 19.9%. In 2014, the figures changed to 10.3% and 11.4% respectively. Processing generated USD 27.4bn in gross value added, while agriculture brought only USD 9.3bn in 2007. In 2014, the figures changed to USD 13.5bn for processing and USD 15bn for agriculture.

In 2014, the food sector accounted for over 26% of the total output in the processing industry. This made it the largest sector outrunning even, for the first time ever, the steelmaking industry at slightly under 25.8%. The trend becomes even more obvious when looking at Q4 2014 (27.8%) and January-April of 2015 (25.3%), when the State Statistics Bureau stopped taking into

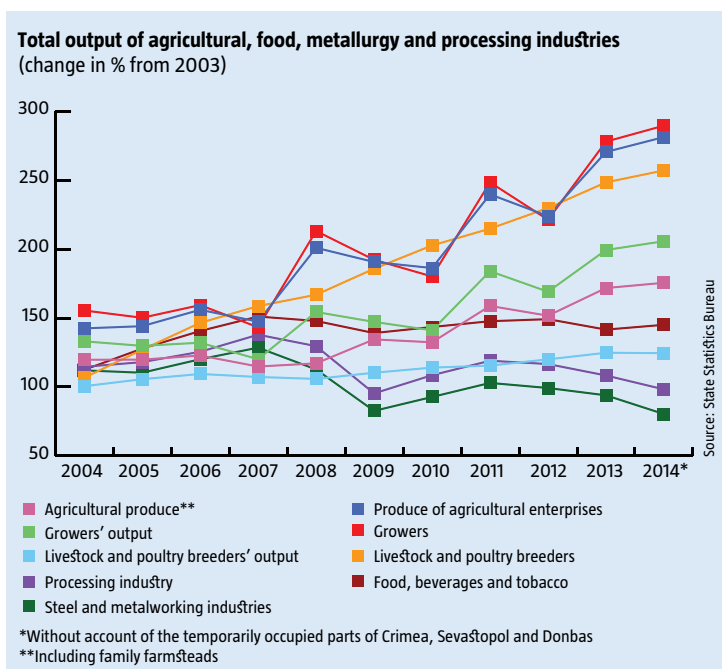
account the occupied parts of Donbas. The branches that make food products (agriculture and food processing) already today generate at least 1.5 times more gross value added than all other processing industries taken together.

Employment dynamics in the agricultural industry is similar. In May 2015, it employed 432,100 people (without account of microbusinesses and individual entrepreneurs, the latest data on which available for 2013 state 92,300 employees, including Crimea and occupied parts of Donbas). Another 290,500 were employed in the food industry. This amounts to the total of 722,100 employees. The rest of the production industry (excluding food sector) employed 1,045,200 people (without account of microbusinesses and individual enterprises, which in 2013 employed 195,500 people, including food industry). Split by sectors, 237,700 people were employed in the steel industry, and 348,600 in machine-building. At the same time, the agricultural sector also had about 40,000 farming enterprises and over 320,000 family farms using agricultural equipment in their businesses, not to mention another 3.8 million private farms that for the most part are involved in semisubsistence farming.

Over the past decade, it was agriculture (mainly its finished goods sector) and, to a lesser extent, food industry overall that showed the most successful dynamics in terms of both output and labor productivity. From 2003 to 2014, agricultural output grew 75.6%. This was primarily due to the 5.3-times growth of labor productivity in the agricultural produce sector between 2003 and 2013. For comparison, over the same period, output in the processing industry shrank 1.8%. The food industry saw a significant increase in output (45.1%), though modest compared with agriculture, while output in the steel industry declined 19.7%.

Such changes in the structure of the economy affected Ukraine's position in the global division of labor, and responded to global demand for various products that the Ukrainian economy could offer based on its natural competitive advantages. While in 2008, food exports from Ukraine constituted USD 10.82bn or 16.2% of USD 66.95bn of total exports, in 2014 the share reached USD 16.67bn, or 30.9% of the total of USD 53.9bn. Exports in the steel industry — once the main export earner — shrank by about USD 11bn over the same period (from USD 26.5bn, or 39.6%, in 2008 to USD 14.6bn, or 27.1%, in 2014). Exports in machine building decreased by more than USD 3.4bn (from USD 10.9 bn, or 16.3%, to USD 7.36 bn, or 13.7%).

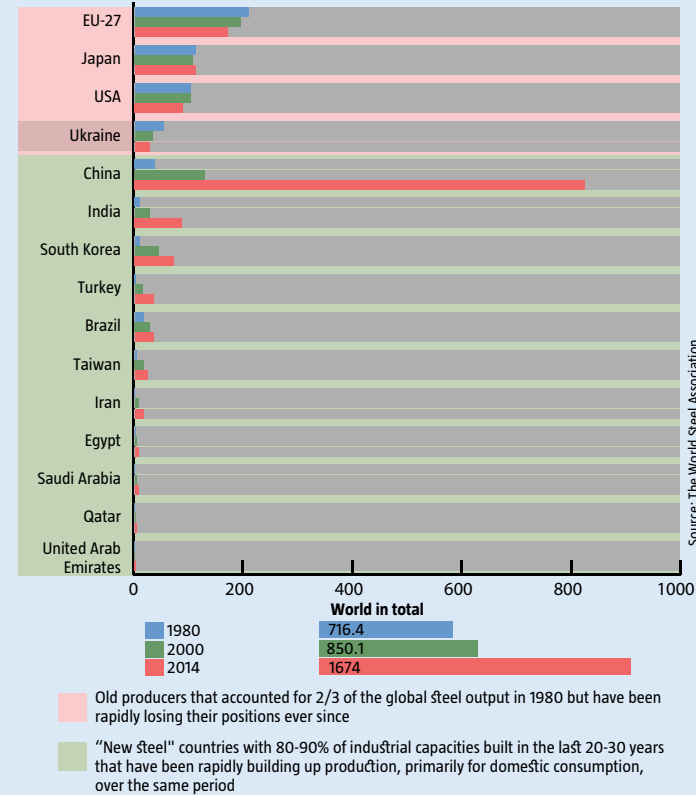
The trend became more pronounced in 2015, when the loss of the occupied parts of Donbas demonstrated its full effect. In Q1 2015, Ukraine exported



Losing market for steel

Ukraine remains one of the largest net exporters of steel products, 70% of its output heading for exports. By contrast to agribusiness, however, the prospects of Ukrainian steel industry in the global markets look dim: outdated local plants can hardly compete with new enterprises built in the developing countries in the past 10-20 years

Steel output over the past 35 years, mn t



USD 3.44 bn worth of food products, or 36.5% of total exports (USD 9.42bn). In Q1 2008, the share of food products was a mere USD 1.79, or 13% of USD 13.79. Exports of the steel industry shrank over the same period from USD 5.62bn, or 40.8% of total exports, to USD 2.46bn or 26.1%. Exports of machine-builders fell from USD 2.4 bn or 17.4% of the total to USD 1.03 bn or 10.6%.

The prospects for Ukrainian steelworks and machine-builders in their current form look dim. This gives reason to expect further reduction of their share in favor of food production in Ukraine's economy and exports. Still, despite their losses, metallurgy and machine building remain disconnected from the needs of the domestic market and rely on exports by 60-90%. For example, in January–April 2015, 69% of Ukrainian steelwork products, including 70% of steel, cast iron and ferroalloys and 67.4% of pipes were exported. In machine building, 90.2% of parts and accessories for motorized vehicles, 68.5% of locomotives and train cars, and 73.1% of general purpose vehicles were exported. Their competitiveness on foreign markets is plummeting for obvious reasons.

Global steel production has doubled from 0.85 bn tons in 2000 to 1.67 bn tons in 2014. It increased in China by nearly 700 mn tons (from 128.5 to 822.7 mn tons), in India by 60 mn tons (from 26.9 mn tons), in

South Korea by 28 mn tons (from 43.1 mn tons), and in Turkey by 20 mn tons (from 14.3 mn tons). Meanwhile, in a number of the Middle East countries it grew 2.5-3 times or even tenfold (**see Losing market for steel**). This was due to the development, in the past 15 years, of modern steel production capacities that mostly focus on extensive domestic markets (in most of the above countries), and/or to cheap energy (in the Middle East). The "old steel" countries where production facilities had been built over 50-100 years ago and since underwent only partial overhaul at best, saw continued reduction or stagnation of production (EU countries, US, and Ukraine).

With this in mind, Ukrainian steel industry that sells 70% of its products abroad has no sufficient competitive advantage in the long run—neither over the "new industry" countries that have modern plants with much higher efficiency, no need for major upgrades in the near future, and focused on large domestic markets for 80-95% of their output; nor over the rich "old industry" states that have cash to invest in modernization and means to protect their domestic markets, to which their steel manufacturers mainly sell. Ukraine's domestic market needs only about half of the industry currently produces (surplus products could be exported after domestic demand is met). The revival of Ukraine's machine-building is only possible after a comprehensive reboot including shutdown of most plants that produce goods uncompetitive outside of the Eurasian Economic Union and the establishment of new facilities oriented on the extensive domestic market, as well as on foreign markets.

In this context, besides the potentially promising new sectors such as IT, it is agriculture that will most likely determine the growth of Ukraine's economy and its place in the global division of labor in the decades to come. This will require deep changes to the Ukrainian mindset.

STEREOTYPES AND REALITY

Under the influence of the long years of Soviet propaganda based on the realities of the 19th and the early 20th century, a stereotype was imprinted in the minds of Ukrainians that agro-industrial countries are doomed to be poor and backward, and that agricultural exports come from the Third World countries that are seen exclusively as raw material suppliers to the advanced and the rich that do the processing and consumption. The 21st century reality is quite the opposite. The share of agribusiness in general and of growers' output in particular in the economy and employment of a country depends not only on its wealth or level of development, but primarily on its potential to manufacture these products. Whereas industrial goods (from clothing to steel and electronics) may be produced for imported raw materials anywhere from Korea and Turkey to Saudi Arabia, the UAE, the Philippines, Vietnam or Bangladesh, agricultural products can only be grown in the countries with suitable lands and climate.

According to the data of the Food and Agriculture Organization of the United Nations (FAO) for 2011 (the latest comparative data available on its website), among the top twenty leading exporters of wheat there is just one poor country, Pakistan, with sym-

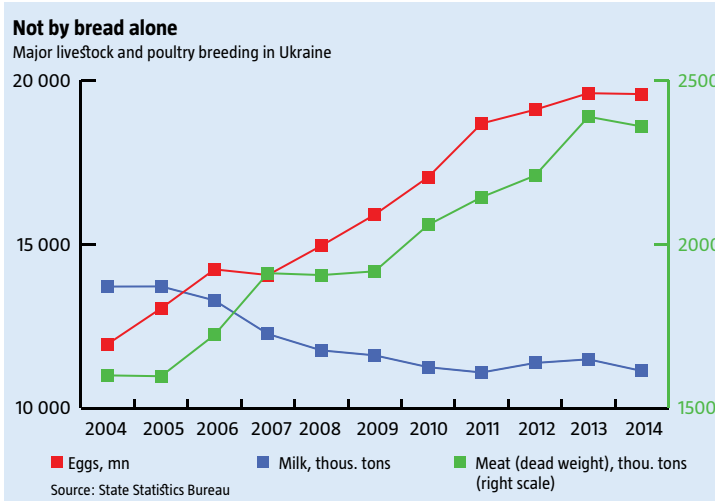
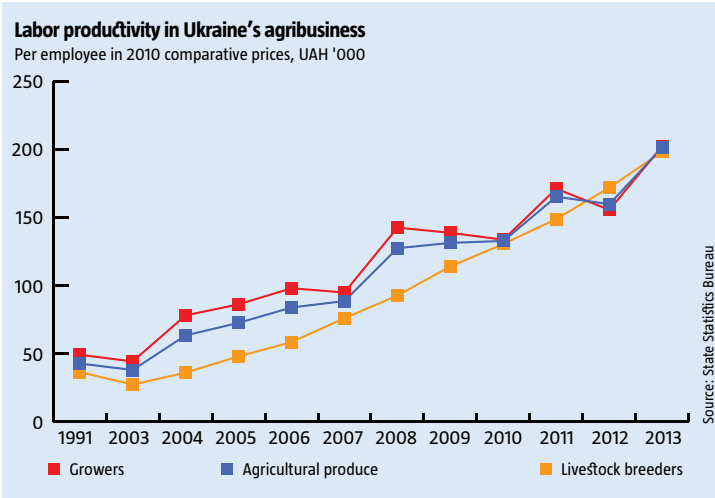
bolistic export volumes of 2.1 mn tons. GDP (PPP) per capita of the rest (except for Ukraine) was at least not lower than that of the poorest EU member-states. A similar situation is in corn exports, which today take the first place among all grain exports from Ukraine. In global rankings, Ukraine has risen to the second and third places (with 19 mn tons in 2014/15 marketing year) from the 4th place in 2011. The list of the top ten sunflower oil exporters again is far from the concept of poor or backward countries: Ukraine, Argentina, France, Netherlands, Russia, Hungary, Turkey, Romania, and Belgium. On the list of rape exporters, Ukraine finds itself in the company of Canada (7.9 mn tons), France (1.7 mn tons), Australia (1.55 mn tons) and the UK (0.66 mn tons). Recently, Ukraine has been rapidly increasing poultry exports (175,000 tons in 2014), but there are no countries poorer than Ukraine among poultry exporters, the top ten of which include the US, the Netherlands, France, Belgium, Germany, Turkey, Poland, and Argentina.

Let's now look at the food export structure of the global leaders. The US exports soybeans (USD 17.6bn), corn (USD 14bn), wheat (USD 11.1bn), cotton (USD 8.4bn), pork (USD 4.7bn), poultry (USD 4bn), cattle (USD 4bn), and soybean meal (USD 2.7bn). Canada exports rape and rapeseed oil (USD 8bn), wheat (USD 5.7bn), pork (USD 2.3bn) and soybeans (USD 1.4bn). The structure of food exports of the major European exporters is somewhat different. For example, in the structure of French exports, wine takes the first place (USD 9.9bn), alcoholic beverages the third (USD 4.5bn), and cheese the fourth (USD 3.4bn). However, top five exported French food products also include raw wheat (20.3 mn tons, or USD 6.7bn) and corn (6.2 mn tons, or USD 2.5bn). Besides, France exported rape and rapeseed oil (USD 2bn), barley (5 mn tons, or USD 1.4bn), and poultry (0.43 mn tons, or USD 1.1bn).

UKRAINIAN AGRIBUSINESS POTENTIAL

In the countries that are comparable to Ukraine by their agricultural potential, agriculture generates much larger shares of GDP. In Canada its share in GDP is more than USD 35bn, in Argentina USD 45bn, in France USD 50bn, and in Australia USD 60bn. In Ukraine, this figure is still below USD 17bn. Argentina is the poorest country on the list, but the share of export-oriented agroindustrial complex (the share of food exports is over 50%) in its PPP GDP per capita in 2014 was USD 22,600. This is comparable to Poland (USD 23,700) or Hungary (USD 22,900), the level that Ukraine can only dream of in the next decade.

Ukraine, despite being geographically located in Europe, is closer to Argentina, Canada and Australia in terms of its agricultural potential per capita. Today its agricultural holdings and farm businesses employ about as many people as does the highly mechanized agricultural sector of the UK (535,000), despite the fact that Ukraine has much vaster agricultural lands: 2.5 times more farmlands and 5.5 more croplands. For another comparison, Ukraine has almost as much arable land as France and Germany combined, but 3.6 times less population and at least 4.5 times fewer people employed in agricultural production (without account of homesteads).



Moreover, while the share of agriculture proper in GDP and employment in most developed countries is usually 2–5%, its share in agroindustrial complex hits 20–25% or more. The latter traditionally has three main components. The first one is cultivation. The second one is gathering, storage, transportation, processing and selling agricultural produce and food goods. The third one includes industries production of capital goods for agriculture and food sectors (agricultural, livestock husbandry and food processing equipment, fertilizers, compound feed, bioindustry products, and construction of farming facilities).

Ukraine today is realizing, to some success, its potential in the first of these three components. Ukrainian growers were the first to enter the global market. The production and exports of grain, oil-yielding crops and their derivative products has placed Ukraine on the list of the top producers of some goods. In 2014, grain harvest reached the record of 63.9 mn tons compared to 41.8 mn tons in 2004. Exports in 2014/15 marketing year (lasting from July to June) amounted to 34.4 mn tons vs. 11.4 mn tons in 2004/05. The actual growth was even bigger, since the data for the year 2004/05 include the occupied parts of Donbas and Crimea statistics. It is absent from the data for 2014/15. The potential of Ukrainian crops is still very

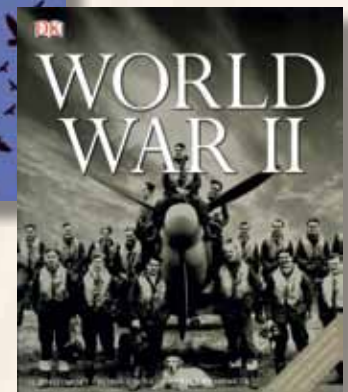
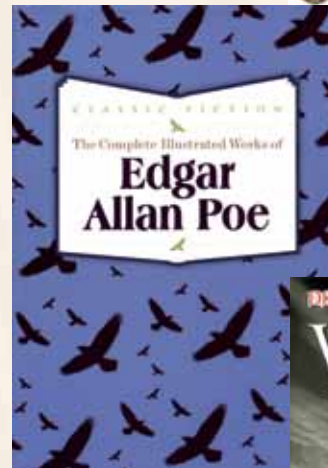
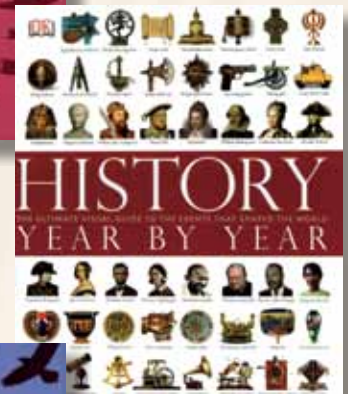
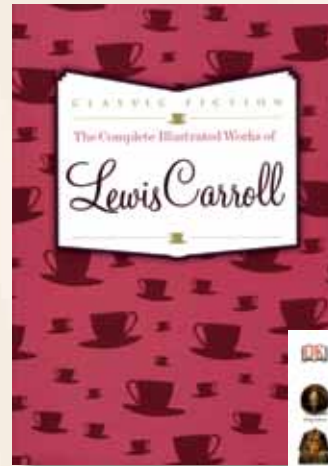
high compared with the rest of the leading global players. Land under cereal production in Ukraine (14.9 mn hectares) is comparable with that of Canada and Australia and is more than 1.5 times larger than those of Argentina and France.

However, despite the widespread stereotypes, the last decade saw a rapid growth not only in crops or oilseeds harvesting, but also in livestock breeding. In 2004-2014, according to statistics, the production of meat grew 1.5 times (from 1.6 mn to 2.4 mn tons) and the output of eggs increased more than 1.6 times (from 11.96 bn to 19.59 bn), but the actual growth rate was even higher, as the 2004 statistics include Crimea and occupied parts of Donbas. The growth was due primarily to the businesses producing finished goods.

The progress in the production and exports of poultry is especially manifest: domestic manufacturers not only replaced imports, but also made this sector of the Ukrainian economy export-oriented (almost one third of all domestically produced poultry today is exported). Egg production is also becoming increasingly export-oriented. Recently, the largest Ukrainian egg manufacturer, Avangard holding, announced the intention to increase over three to five years the share of exports in its sales to 50-60% compared to the current 20-25%. Ukraine's prospects also look good in the dairy sector. While cheese exports are still going through a crisis after the loss of the Russian market, the exports of butter, condensed and noncondensed milk and cream have resumed growth after entering the new markets of the Mediterranean and the Middle East. For example, the main importers of Ukrainian butter today are Egypt, Morocco, and Azerbaijan.

The first component of the agribusiness industry (cultivation), with its successful growth dynamics, is performing significantly better than the second and especially the third components. The lack of efficient storage, processing and transportation capacities results in significant annual losses for Ukrainian agriculture and hinders its growth, making it necessary to import fruits, berries and vegetables instead of exporting them in the off-season period. The situation in the third component is rather critical: Ukrainian agribusiness largely depends on the imports of most machinery and equipment used for agricultural production, cattle breeding and food processing, as well as components, seeds, crop protection agents, fertilizers, etc.

This is the evidence, on the one hand, of the problems existing in the sector, and on the other hand, of its significant potential for production and employment through import substitution in case modern jobs with high labor productivity are created. In this case, the share of agriculture and related industries in GDP and employment, despite high mechanization and labor efficiency, may be several times higher than in the European countries. The key to success here is focusing primarily on the competitiveness of Ukrainian producers that need no subsidies in global markets. Ukraine has all the prerequisites for this. Otherwise, Ukrainian agribusiness may become a burden on the country's taxpayers and other industries, only becoming heavier with the growth of production and employment, instead of being one of the locomotives of the national economy. ■



Jean-Jacques Hervé:

“When the community demands a responsible attitude to its land, it is a sign of democracy”



PHOTO BY ANDRIY LOMAKIN

Interviewed
by
**Anna
Korbut**

The *Ukrainian Week* spoke to the French expert, former Counselor to the governments of Russia and Ukraine for agriculture, who has spent the last ten years working in Ukraine, on the pros and cons of lifting the moratorium on land sales, the role of large agricultural holdings and key factors in the development of Ukraine's agricultural sector.

A few years ago you said that Ukraine was not ready for the sale of land. Has the situation changed since?

I believe that there are still no preconditions to lift the moratorium. Today no one knows exactly how many hectares of land are under lease (besides, there are three categories of land: state-owned, municipal, and private). It would seem that basing on Soviet records, we should know exactly where the land is and how much of it is available, but this is not the case. Given the corruption in the responsible departments, no one is ready to say clearly what land is where. This means that an inventory audit should precede any sale.

In addition, several laws should be adopted. In particular, holding companies that have not been paying due rent for the use of public land should pay back the outstanding sums. The mechanisms for determining the value of exploiting such resources are available. If they cannot pay their debts now, it's not a problem: they could pay them by installments in 5 or 10 years. Also, it should be clearly determined who is renting which allotments of municipal land resources. I am sure that even

old Soviet documents would come in handy for that end. Next, it is necessary to define plots of land owned by an individual not just as an abstract allotment of a certain size, but as a percentage of the entire field. For instance, when people privatize apartments, no one knows who owns the stairs, elevator, basement, or pipes, and therefore no one is willing to repair them. Would it not be better if each owner owned a part of the building proportionate to the size of his apartment and paid the annual amount required for its maintenance? It is the same with the plots of land.

Finally, when people have titles to plots of land, assigning a field or a land plot for the use of, say, an agricultural company should require consent of 50% + 1 or more owners. In France, the terms are somewhat different: to assign resources into a company's use, consent of 50% of individuals who own at least 75% of the land in question is needed, or of 70% of those who own at least half of it. The difference with Ukraine is that people here have more or less equal land plots. Therefore, these proportions may be defined differently, but there should still be a law to regulate that. Companies competing for the right to be assigned these allotments by the community for their use should make their respective offers: pay less per hectare of meager soil, but more per hectare of good soil, plus an obligation to repair a church or a school for the community. In this way, the owners of land plots can choose an offer they prefer.

Of course, there is the risk of corruption schemes. No doubt, it will take about three generations to get rid of corrupt officials. However, the first step needs to be made. It's like climbing Hoverla: the route is easy and fast at the beginning, and the most difficult stretch is near the top.

Given that land in Ukraine is the source of corruption, how can we make sure that after the inventory is taken, the land does not end up in the hands of latifundist monopolies or companies exploiting resources irresponsibly, whereas small and medium sized agribusinesses, having no access to credit and no political leverage, will be barely surviving?

I think, if I were a Ukrainian official, the first thing I'd consider would be how efficient enterprises are. These can be found among both large and small businesses. Inefficient companies should not stay in business. Banks have these criteria to decide whether to grant a company a loan or not. There are enough specialists today who can evaluate the performance of a company. Another indicator for me is the number of jobs created by a farm. Almost 8 million people willing to work live in rural areas (as is evidenced by the number of individual household farms). Another criterion is how an agriholding supports village life: schools, clubs, and culture.

So, I would primarily support a company with the best results by these three criteria. However, Ukraine today already has a high unemployment rate, and there's no point in increasing it further by closing down imperfect companies. They should be receiving support over a certain time period. Cooperation between businesses should also be promoted. For example, there are some very large holding companies keeping up to 10,000 cows and having laboratories and other resources. Maybe small villages could use their potential? It might never have occurred to those small farmers before, but the task of a skilled manager is to direct them. Overall, I think you should start with what you have: large fields that existed even before the Soviet times; people living in villages who have always worked on the land; and managers who know how to manage a business. Some of them work honestly and very well, while others only care about money. Such people should be kept away. Today they work in agriculture, tomorrow in some other business. In this business, however, stability is necessary.

Do you have the impression that the officials responsible for agriculture and the country's government will be willing to listen to expert opinion and consider the best practices for the Ukrainian market?

I think, the current Minister will listen. In late March, the Presidential Administration urged to speed up the process of land sales, but he said that the inventory should be taken first, and the last stage of creating a digital land registry should be completed.

What should be the ratio between land resources owned (or leased) by large agricultural holdings and small and medium-sized farms for the best stimulation of the economy and the development of rural areas?

To answer this question, we must compare productivity and effectiveness of large enterprises. This should be the work of scientists: to consider a wider range of data than the State Statistics Bureau does.

However, I do not support holding companies that are managed by only one person or family, without turning to professional managers. Such enterprises cannot be stable and have regular customers, they will not stay in operation for longer than 5-10 years. Let's say, in France, Germany, USA or Canada, one farmer manages about 20-40 fields (5-10 ha each) owned by a company. He tries to minimize the cost of capital investments and employee work time required to perform a task. The normal amount of land for a company, to my mind, should not exceed 3,000 ha. If operations are successful, it can be doubled, but operating more than 7,000 ha is unrealistic. For that end, it would be better to establish partnerships, international cooperatives and so on. Cooperation within such establishments is advantageous for strengthening market positions and minimizing costs (from the perspective of scale economy).

If they can perform, let them work. However, their structure has to be inspected. Besides, they have to prove their efficiency and pay normal taxes. In the meantime, I understand that some people today spend more money on bribes than on taxes, and this needs to be dealt with.

How do you assess the potential of Ukraine's agricultural sector?

It is great. There are areas where production may be mechanized. And there is a constant demand, be-

Jean-Jacques Hervé is an expert on agriculture and agribusiness and foreign member of the National Academy of Agricultural Sciences of Ukraine (2010). His work experience in the industry totals 43 years. Until 1992, he held the position of a civil employee at the Ministry of Agriculture, Agrifood and Forestry of France; in 1992-1996, he headed the National Agricultural Institution of Higher Education of Dijon, France (ENESAD). In 1997-2003, Mr. Hervé served as Counselor on agricultural matters of the economic mission with the French Embassy to Russia; in 2005-2009, Counselor to the Government of Ukraine on agricultural matters. He is member of the Russian Academy of Agricultural Sciences (2003), the French Academy of Agriculture (2006), and Advisor to the Chamber of Commerce of Burgundy.

cause the number of people who need to be fed is constantly increasing. When I started working here 10 years ago, Ukraine exported not more than 8-10 million tons of grain. Today, it could export 40 million tons, i.e., five times more, after only a decade. There are, of course, problems with transportation and logistics infrastructure, but they are not critical and can be solved. In another ten years, you could be exporting 100 million tons.

Besides, in Ukraine the difference between the farmer's cost and FOB price is twice higher than in France. Why? Our countries are similar in size, we have slightly better roads, but your drivers are used to work on what you have. There are trains, even though they are slow. There are barges that could navigate the Dnieper. That is, a larger share of this margin could go to the manufacturer. If he gets a higher profit, he will have something to invest in business development. Out of the 50,000 companies that have survived in Ukraine even under current conditions, most are working with little or no support, and some have even subsidized other sectors of the economy, all the while ensuring productivity growth. Their managers have been to various countries and understand what should be bought where. I am sure that out of those 50,000, at least 20,000 are very efficient.

Talking about the processes that took place in Canada and the United States a century ago or in France and Germany after the World War II, we tried to help talented potential farmers start their businesses. In the Netherlands, they had an even more efficient experience: they trained farmers in good practical education institutions — not universities, but with a good level of education — and assigned polders, or drained low-lying tracts of coastal land, for farmers to work on. If within three to five years they demonstrated the expected results, they continued to work. If not, they got a few warnings before the land was taken away from them. They could also buy land. So, let's go back to the first question: why sell all the land now? After all, it will grow in value gradually and constantly...

And this is not just about agriculture. If an agricultural company is willing to do something for the community, it will take care of schools and cultural institutions, and other small businesses can work alongside. Tourism potential may be developed in a similar way: being a farmer, I can build a stylish comfortable house where tourists could come, and use the proceeds to repair other buildings. This, incidentally, is a very important component of agricultural development in the EU. When the community demands from the company working on its land this kind of a responsible attitude, this is another sign of democracy. ■

Slow Out of the Gate

Lyubomyr Shavalyuk

An overview of Ukraine's new tax system

Tax reforms are still under construction in Ukraine. As planned, they should come to fruition with the institution of a fundamentally new tax system starting January 1, 2016. Prior to that, the planned reforms will also have to get a green light from the Verkhovna Rada, which is supposed to get the necessary bill to debate and vote on by the end of autumn. At this time, key elements of this new system are being discussed in expert circles. And although the press is receiving precious little information about the changes to the tax system, tax specialists have already worked up quite a few elements. From them, we can begin to piece together an outline of Ukraine's future tax system.

THE CHANGE-IT TEAM

Tax reform is one of the key factors to improving the investment climate, whose potential impact on economic growth in Ukraine is hard to exaggerate. Without any doubt, Finance Minister Natalie Jaresko, who has been put in charge of this transformation, understands this very well. She is currently in charge of the Tax Reform Task Force, which is collecting all propositions for changes coming from civil society, analyzing best practice in other countries, adapting them to the circumstances in Ukraine, and working up a model that will work best for this country.

In effect, the Task Force is where the decisions regarding tax reforms are being made, decisions that will determine how business-friendly the new system is and how effectively it fosters economic development. The way the work of this team is organized so far has a number of pluses and minuses. The first obvious plus is that it includes more than just fiscal experts. Of its 20-odd members, only 3 work in the State Fiscal Service (SFS), another 3 work in the Economy and Finance Ministries, and 5 are members of the Verkhovna Rada. Clearly the Government has learned a lesson from last year's farce, when the only people involved in changing the Tax Code were from the State Tax Administration and produced a predictable result that effectively included no systemic changes. In short, there is a good chance that the position that President Poroshenko presented in his State of the Nation address before the Verkhovna Rada—that the focus on taxes needed to be switched from their fiscal function to their incentivizing one—will be implemented.

Secondly, the team includes foreign advisors who not only have in-depth understanding of the nature of successful tax reforms in other countries but, such as former Slovak Deputy Premier Ivan Miklos, actually initiated transformations of this nature and personally put them into practice in their own countries. Their experience will clearly stand in good stead.

Thirdly, the task force includes 5 representatives of civil society and the business community, including the largest associations of foreign businesses in Ukraine: the

European Business Association (EBA) and the American Chamber of Commerce (ACC). This means that the opinions of both society at large and business in particular will be heard, something that has so far been a very rare occurrence in Ukraine.

Among the flies in the ointment of the Task Forces' approach, two stand out. For one thing, it also includes two representatives from the IMF, which means that radical reforms that might lead to short-term losses in terms of filling the Treasury but might translate into stronger economic growth in the three- to five-year perspective are not likely to happen. The IMF will not support any initiative that might create additional risks to budget revenues. On the other hand, the representation of foreign businesses in the shape of the EBA and ACC without direct representation of domestic businesses—one might be glad that the oligarchs aren't represented, although some of the MPs could indirectly be promoting their interests—could result in a concept for the new tax system that is too skewed in favor of foreign business.

In short, the Tax Reform Task Force's work could either bring exceptional results or extremely unsatisfactory ones. It includes fiscal specialists who know the system from within, but may not know what it should be like; civil society, which has a good idea of the kind of tax system the country needs, but doesn't always understand the instruments with which this might be achieved; foreigners who have a good sense of the nuances of the best tax reforms, but do not know much about how things work in Ukraine; deputies who will likely inject some elements of populism, which will likely get the rest of the team up in arms. If all these sides prove to be a good fit, the results should be very good. But if



REFORMS TO THE TAX SYSTEM NEED TO GO HAND-IN-HAND WITH REDUCED BUDGET EXPENDITURES, TRANSPARENT STATE PROCUREMENTS, AND REDUCTION OF CORRUPTION AMONG BUREAUCRATS

they deliberately become destructive, then none of these groups will be able to launch the right kind of tax reform, no matter how much they might want it.

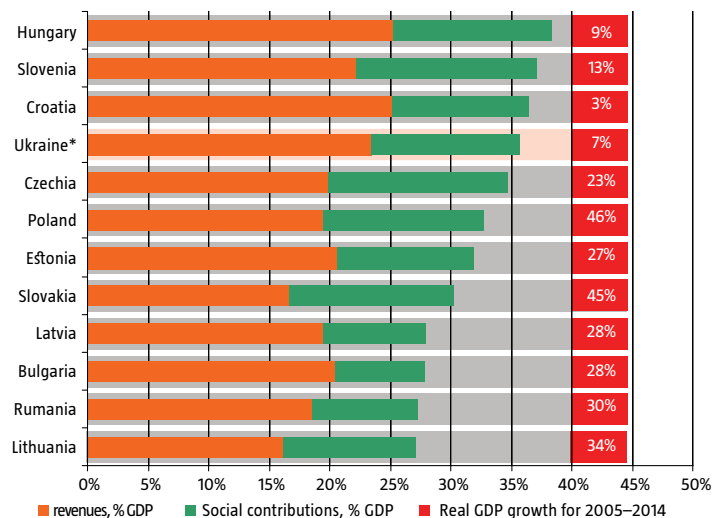
PRESSURE POINTS

Ukraine's new tax system needs to be based on a number of principles that work well in other countries, while not rejecting certain principles that acknowledge the way things are in this country.

Paradoxically, some key tax reform success factors are beyond the country's reach right now. For instance, last year's Global Competitiveness Report ranked

Taxing competition

In most CEE countries, a far smaller share of GDP is distributed out of tax revenues and social contributions than in Ukraine. The less business and individuals have to pay, the faster the domestic economy grows.



*Data for tax revenues and social contributions for Ukraine from 2014; for other countries, from 2013.

Sources: Eurostat, Derzhstat, the State Treasury and extrabudgetary funds, author calculations

Ukraine 138th among 144 countries for wastefulness—read, embezzlement—in budget spending. The immediate impact of this is that Ukrainians trust neither the government nor government officials and so they don't pay their lawful taxes, justly arguing that the money won't be put to proper use anyway. In this kind of situation, even ideal tax reforms will not succeed if the state fails to learn to manage taxpayer contributions in an efficient, thrifty manner, because ordinary Ukrainians will continue to distrust it and not pay taxes.

This means that reforms to the tax system need to go hand-in-hand with reduced budget expenditures, transparent state procurements, and a maximal reduction of corruption among bureaucrats, who are, after all, hired by the public and whose salaries are paid for with taxpayer contributions. For the new tax system to become effective the minute it is launched, Ukraine needs to also complete the lion's share of other, no less important reforms simultaneously, by the end of this year.

Another cornerstone to effective tax reforms is changing the mentality of tax and customs personnel. As in most developing countries that also have a totalitarian past, people in these professions effectively belong to the policing arm of government, wear uniforms with epaulettes, and so on. Typically, their attitudes fall into two categories: either "All businesses steal from the state whose interests we tirelessly defend, so we put pressure on them..." or "Anything can be arranged for the right sum of money or orders from above." They have no awareness that they are hired by their society and are supported at public cost—and never did.

In short, reform needs to not just filter out the personnel in the State Fiscal Service, within reasonable limits that still need to be determined, but the entire tax system needs to include mechanisms that ensure that both ordinary Ukrainians and businesses are protected from the arbitrariness of tax and customs officials. This

means reducing contact between taxpayers and inspectors to a minimum, reducing the number of inspectors, so that they are busy doing their job and not wandering around collecting bribes, setting legal limits on the timeframe and number of inspections, both planned and irregular, and other measures.

The main purpose of tax reform is obvious: reducing tax pressure on business. But this can be interpreted in a variety of ways. Macroeconomically, too much of GDP goes to tax revenues and social contributions in Ukraine, leaving both business and ordinary citizens with fewer financial resources. This deficit makes it impossible for the economy to recover properly.

Figure 1 clearly illustrates that, among Central and Eastern European countries, those that put a smaller share into taxes and fees generally develop faster. This is the main macroeconomic factor that needs to be taken into account as Ukraine reforms its tax system. This makes Ukraine's tax system uncompetitive even at the regional level, never mind globally, when investors have plenty of countries to choose from among Ukraine's neighbors, with their less burdensome tax systems. To change this around, Ukraine needs to reduce the tax burden to 7–8% of GDP or about 20–25% less than what it is now.

This means radically reducing budget spending in two main areas. The volume of embezzled or poorly spent public funds needs to be radically diminished—although this alone would not be enough—, which can only happen with radical, all-encompassing reforms. Certain state functions need to be eliminated (making education and healthcare largely private and pay-as-you-go is one option) and build the state on a liberal basis. This second option was not common in Ukraine and certain diehard paternalists, of whom Ukraine has its fair share, only need to hear the whisper of such an option to immediately set up a huge hue and cry. Ukraine really must make a choice for itself: either paternalism and the eternal cycle of poverty, or a smaller state and a booming economy. There is no "third way."

Globally, the situation looks something like this. Based on the 2015 Doing Business Index, the indicator for "Paying taxes" puts Ukraine 105th out of 189 countries; for "International trade," Ukraine is a dismal 154th, suggesting that the Customs Service needs even greater reforms. Moreover, the tax rating indicates that businesses in Ukraine pay an average of five payments a year, spend 350 hours to complete any number of reports for the payment of taxes, and are taxed 52.9% on profits. In countries in the top places, such as Qatar and the UAE, taxes are paid quarterly, reports take 41 and 12 hours to complete, and the profit tax rate is 11.3% and 14.8%. The top 30 countries, which is where Ukraine should find itself in another five years according to Strategy 2020, end with Brunei, a tiny southeast Asian country where businesses make 27 payments a year, spend 93 hours to fill out declarations and make payments, and pay 15.8% on their profits. These key points make it clear that Ukraine needs to reduce the amount of time and money spent on taxes severalfold. Only then will the country's investment climate become globally competitive. If we consider the corruption component and include the money spent building the palaces that the Tax Administration has built itself in just about every county of Ukraine—to say nothing of the personal palaces that tax officials have built for themselves—, the room for improving efficiency through tax reforms is virtually unlimited. ■

CONSTRUCTIVE CONCEPTS

At this point, the tax reform bill is under constant negotiation. Reforms.in.ua consolidates all the latest information and posts suggested changes from 10 different parties, some of whom have presented 2-3 documents. Some of the proposed innovations have been unanimously supported by all the participants and these will most likely go through in the end.

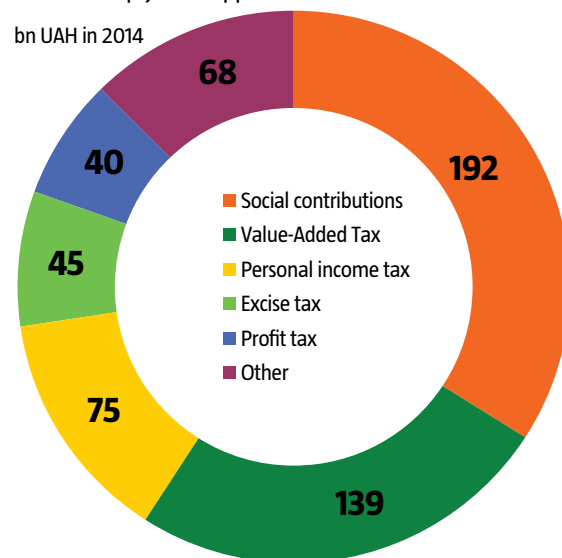
Most of the experts and quite a few of the business owners agree that the administration of taxes is a much bigger problem in Ukraine than high tax rates. In other words, the way tax inspectors interact with taxpayers needs to be reformed far more than taxes per se or tax rates. This, in fact, is the most complicated aspect of reforms and the most challenging task facing Ukraine's reformers. In order to attain a balance that would prevent individual tax officials from interpreting legislation as they please, to demand a bribe or to power trip, while taxpayers get to pay a fair rate, the system needs to be changed from within. At the same time, it has to be "sequestered" from the process in order for its flaws to be seen from the outside. To expect any one individual to be able to do all this is unrealistic. And that's why the Task Force needs to bring together professionals from different spheres.

One group of experts proposes adopting the Estonian model of profit tax. The essence of it is to not tax the entire profits of a company but only those that are distributed as dividends and other payments. This immediately removes a number of problems. Firstly, if the owner puts everything earned into growing the business, then no taxes are owed. This is good for the company and it stimulates economic growth. Secondly, the issue of double taxation is resolved, where the company first pays profit tax and then is taxed again on dividends. Thirdly, there's no reason to hide profits or move them offshore because as long as they aren't distributed, they aren't taxed. In the worst case, they aren't used for investment but lie around in the corporate bank accounts, that is still good for the domestic banking system. Fourthly, this effectively eliminates the need for tax accounting, simplifying the entire system. Specialists from the Reanimation Package of Reforms (RPR) have promoted the radical notion of eliminating tax accounting altogether by instituting the Estonian style of profit tax.

The value-added tax or VAT presents an entirely different set of problems. Some in the Task Force think it should be dropped altogether, because it is the source of the most abuse and provides ample opportunities for corruption. But this is not so simple. According to Eurostat, the EU statistics agency, Central and Eastern European countries the VAT or its equivalent ranged from Slovakia's 21% to Croatia's 35% of all tax revenues and social contributions ranged from 6.4-12.6% of GDP. In other words, this tax is typically a budget filler. Ukraine is very much in line with its neighbors here, as in 2014 VAT revenues were 24.9% of all tax revenues, while social contributions were 8.9%. So, while the VAT can be replaced by some similar tax, such as a turnover tax, but it cannot be dropped altogether without serious consequences. In a country where the tax base for direct taxes, such as corporate profit tax and personal income tax, is exceptionally unstable and amorphous, especially at a time of crisis, indirect taxes perform a critical function as a budget revenue stabilizer. Of

Cutting up the tax pie

In 2014, tax revenues and social contributions were nearly 36% of GDP, which is far too much for a poor country. The lion's share, 88% of this amount, came from just five taxes and fees. This suggests that most of the rest can simply be dropped.



Source: The State Treasury, extra-budgetary funds, author calculations

course, such a move will not change the fact that the state needs to find ways to spend less money on compensation fictional VAT refunds, properly organize its compensation to legitimate exporters, and ensure that the VAT is paid properly, that any schemes to abuse it are eliminated, and so on. Task Force experts have a number of proposals in this regard.

The paradox with the VAT in Ukraine is that of the UAH 139 billion that was collected in 2014, UAH 107bn came from products imported into Ukraine and only UAH 31bn from those manufactured in Ukraine: UAH 81bn paid by domestic manufacturers, less UAH 50bn compensated to exporters. In other words, if this were 50 years ago, the budget could get the same result by simply instituting the necessary import duty. Since Ukraine is now a member of the WTO, this option is no longer available, as Ukraine is obligated to trade with the entire world at a customs duty rate that is no higher than 5%. With EU countries, Ukraine will soon have to trade without any tariff barriers whatsoever, as part of the deal in the Ukraine-EU Association Agreement.

Ukraine can use this to its advantage, of course. By putting the main emphasis on the VAT and reducing income and profit taxes, Ukraine can make imports more expensive relative to the inexpensiveness of domestically manufactured goods, since production cost will now include fewer tax payments for payroll deductions and profit tax. This should incentivize domestic manufacturers and even make them more competitive on world markets, if payroll and profit taxes remain noticeably lower than in Ukraine's competitors. The only "but" is that 11-12% of the VAT tax base is lost due to evasion. If the rate were raised to more than 20%, the share of those evading payments would grow sharply and the real tax base will shrink. How can the VAT col-

¹ SPD is an individual registered as a "subject doing business" so to speak.

² After announcing an open contest for the position where dozens of experienced market-oriented candidates applied, the Cabinet of Ministers appointed Roman Nasirov, a Bloc of Petro Poroshenko MP and head of the Parliamentary Tax and Customs Committee. Nasirov is believed to be a comfortable figure for all political forces and someone who will not clamp down their revenues from corruption in tax and customs systems

lection system be set up to avoid this is an issue that experts still need to think about.

If Ukraine wants to build an economy of the future, based on services and knowledge, then the new tax system cannot survive without the VAT or some other indirect tax. The problem is that such economies are centered on human capital, not on physical capital or goods, and human capital is too mobile for tax administrators and its products are often quite amorphous. In this case, it's hard to effectively tax production and salaries, but consumption is much easier—provided that there is sufficient oversight of sales. Provided that it functions properly, the VAT can help reach this objective.

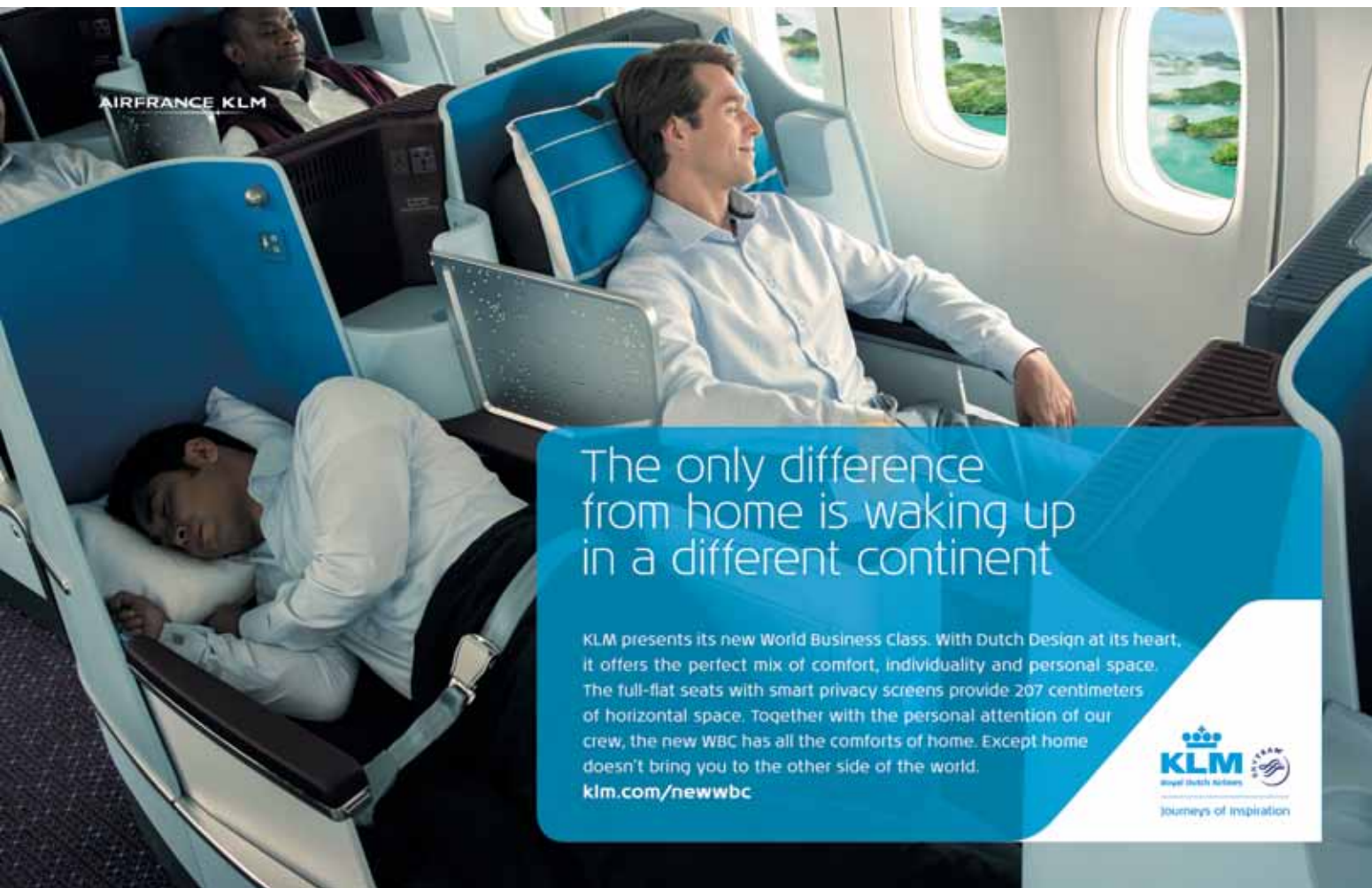
Ukraine's Consolidated Social Contribution (CSC) also needs to be changed. It's too cumbersome for business, even taking into account those changes that were already in effect since the beginning of 2015. As a consequence, salaries are paid out in envelopes everywhere and the use of sole entrepreneurs¹ has shrunk away. At one point, the Minister of Social Policy stated that nearly UAH 200bn in salaries was hidden in Ukraine. In reality, a number of indicators suggest that this sum is likely 1.5-2 times more. This requires radical action. Nova Kraina, a civic platform, has proposed an interesting option: to cap the CSC at the level of the current rate, say 40% of the minimum wage. If it turns out to be true that the shadow economy is about 50% of official GDP in Ukraine—and this opinion is very widely shared—bringing it out of the shadows would completely compensate for any losses from the income taxes of those who earn more. This is effectively a regressive tax that does present some risks for the state

budget, so it needs some more working up. Still, similar calculations indicate that budget revenue losses will be relatively small, while the impact on the tax base will be definitely positive. And once the economy begins to recover, the Government can raise the minimum wage and get more revenue from all those who left the shadow economy behind.

UKRAINE MUST MAKE A CHOICE FOR ITSELF: EITHER PATERNALISM AND THE ETERNAL CYCLE OF POVERTY, OR A SMALLER STATE AND A BOOMING ECONOMY

One of the boldest propositions is to set up a system of individual tax accounts at banks where a percentage of the money coming to a commercial entity's accounts will be set aside automatically. At first glance, this seems very compact and revolutionary, so it merits consideration. Whether it also contains loopholes for evading taxes remains to be studied.

Judging by the overall quantity and quality of the propositions being presented, the debate over the tax reform concept is anything but shallow. Whether this results in an effective, compact and easy tax system, only time will tell. But the main question is whether the country's leadership will find the political will to implement this system. Given who was appointed to head the State Fiscal Service², there are some doubts about this. ■



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Oleksandr Kramar

The direction taken by Crimea's economy destroys its self-sufficiency and makes reintegration into Ukraine exceedingly difficult

It has been more than a year since Russia seized Crimea, the second tourist season under occupation is underway. It used to be the primary source of income for the population when the peninsula was part of Ukraine. *The Ukrainian Week* looks into the way Crimea transformed and continues to transform under the Russian authorities.

What catches the eye from the get-go is the drop in availability of statistical information regarding the economic and social situation on the peninsula since the occupation. The scope and the detail of the statistical data on the Crimean webpage of the Federal State Statistics Service for 2015 is a fraction of what it used to be in 2014 (the local statisticians still used the Ukrainian-standard sheets with all their columns and sections). This considerably complicates the analysis of the social and economic situation on the peninsula. No longer available is the information on the numbers and average income of the Russian military stationed in Crimea, along with the other forces. Moreover the data on the dynamics of production in various areas of economy, actual volumes of particular products, employment by sectors, finally, there is no data on the situation in small business and among those who pay the simplified tax (number of such entities, their staff, production volume etc.).

All of this makes it difficult to assess the state of affairs for the majority of Crimean population, especially those residing away from the central city of Simferopol. Regardless, we will attempt to outline the social and economic situation based on the available data, testimony, publicly available information and expert opinions.

LIVING STANDARDS

In 2013 the average monthly salary of a staff worker in Crimea made USD 350, according to State Statistics Bureau of Ukraine. The March 2015 figure, when calculated using the official ruble exchange rate, is exactly the same. However, there were only 282.1 thousand staff employees in companies, establishments and organizations (not including small firms) in Crimea with population of nearly 2 million. The current overall number of the employed (including self-employed and working for small businesses) in the Crimean economy is something that the official stats no longer provide. Last year this number made 820.6 thousand. Therefore little more than a third of all employed residents are permanent employees, 97.7 of them concentrated in the administrative centre – the city of Simferopol. Its population made less than 20% of the overall population of Crimea. There were only 184.4 thousand staff employees among the 1.55 million population residing outside Simferopol. That's only one in eight residents.

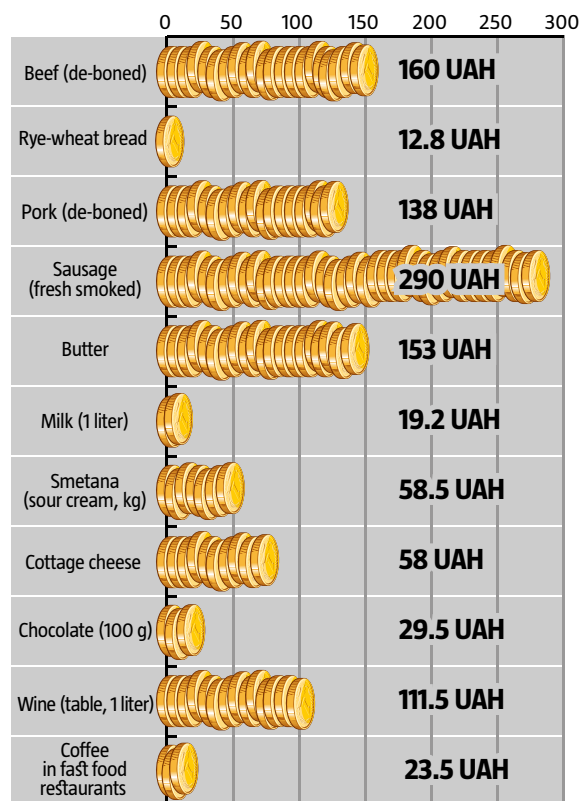
The comparison of the pre-occupation and post-occupation income of the categories (officials, pensioners,

state employees), who are believed to have profited the most from the Crimea's annexation by Russia, shows that it didn't change significantly. The pensioners and the state employees felt barely any improvement, if at all, since Crimea become de-facto part of the Russian Federation. The main culprit here is the prices, which are several times as high as in the continental Ukraine. They increased considerably compared to pre-annexation times even in dollar equivalent.

Exactly how many of the 280 thousand staff employees are currently working for the occupying state is something the statisticians chose not to disclose. Before the annexation 144.6 thousand Crimean residents were employed by administrative bodies, law-enforcement, defence, and the government sector. It is unlikely that this number increased. The opposite is more prob-

Crimean prices

Prices of particular types of goods in Crimea for June 2015 (calculated based on exchange rate of 1 RUR = 0.4 UAH)



Source: Federal State Statistics Service of the Russian Federation

able. In areas with the highest income the employment rate was negligible: only 17.5 thousand in government bodies (excluding local governments), where the average salary exceeded USD 550. High wages were also the prerogative of servicemen, of whom there were several tens of thousands. But, as was mentioned above, statistical data regarding them, let alone their income, has been made unavailable.

Pensioners belong to the second echelon of the occupier state's "clients". There are 540 thousand of them in Crimea. As of early 2014 the average monthly pension made USD 180; it increased to USD 200 by April 2015. Another category is the local government employees and state sector workers. After the annexation their nominal salaries in dollar equivalent have either grown somewhat, or remained stable. Crimean statisticians do not provide generalized data per sector, so we'll have to compare what's available. In March 2015 the pre-school educators got USD 300, comprehensive school teachers – USD 360, higher education teachers – USD 375. In 2013 the average salary in education used to make USD 340. Mid-level medical personnel has USD 305 per month. Doctors and other medical specialists with higher education degrees make USD 480. In 2013 a medic's average salary made USD 315. The income of local government employees in March 2015 made USD 330, while Ukrainian statistics for 2013 provide an average figure of USD 420 for employees of the state administration sector and defence.

We deliberately compared the income level of Crimean state employees with that in the pre-occupation Crimea, instead of the current income in the mainland Ukraine at large or the regions adjacent to the peninsula. After February 2014 Crimea developed separately from the rest of Ukraine with the local prices becoming exceedingly higher than the ones on the continent. The residents of Crimea themselves saw the level of income as one of the most alluring aspects of becoming part of the Russian Federation and are comparing their new level of income with the Ukrainian one that they had before the occupation, and not with the one in the mainland Ukraine after the occupation, which bears no relevance to them.

Foodstuffs, other consumer goods, which are predominantly imports, went up in price after the invasion. For instance, the a kilo of beef on the peninsula now goes for 160 UAH (hereinafter according to exchange rate of 1 RUR = 0.4 UAH), pork – 138 UAH, butter – 153 UAH, cottage cheese – 85 UAH, smetana [Ed. Note: type of sour cream] – 58.5 UAH, rye-wheat bread – 12.8 UAH, 1 liter of milk – 19.2 UAH, 100 grams of chocolate – 29.5-58.5 UAH, coffee in fast food restaurants – 23.5 UAH. Considering the 1.5-2 fold price hike compared to the Ukrainian ones, questions arise regarding the adequacy of the official subsistence level, which for the first quarter of 2015 was set at 2.2 thousand UAH for the employable and 1.72 thousand for the retired. It's even less than currently in Ukraine.

In contrast, the living standards outside the government sector are looking worse not only compared to pre-occupation Crimea, but to the contemporary one in the mainland Ukraine. The monthly salaries of USD 150-250 are lower than those in 2013. And while the real economy is declining (more on this below) the workforce supply is higher than the demand. The hidden unemployment is growing while revenues tumble. The

Crimea's official subsistence level in the first quarter of 2015, in USD according to official exchange rate of Russian Central Bank

The entire population The employable Pensioners



Source: Federal State Statistics Service of the Russian Federation

worst situation is in small business, the data on which is missing in the official Crimean stats for a reason. Back in the Ukrainian Crimea, in 2013 almost 200 thousand persons were employed by small enterprises and private businessmen, which is much more than in the state sector and only 1.4 times less than the entire number of current staff employees in Crimea.

TURNED ON ITS HEAD

Crimea is turning into an exceedingly unsustainable economy, for which subsidies from the Russian federal budget directed at keeping the military and the pension system afloat turn into the prime source of income while the real economy sector and tourism decline.

The downturn in most areas of processing industry is becoming ever more serious: while in 2014 production went down by 11.8% compared to 2013, in January through May 2015 compared to the same period of 2013 it dropped by 24.6%. This is worse than the production drop in Ukraine (if the Luhansk and Donetsk oblasts engulfed in hostilities are to be ignored) for the same period. In spite of the foodstuffs deficit, even the production of meat and eggs is in decline: compared to the first half of 2014 in the second half it dropped by 14.8% and 7.4% accordingly, and by 18.2% and 10.5% in January through May 2015 compared to the same period of the previous year. The tourism industry and the transportation plunged. The transit from the Russian Federation objectively cannot compensate for the losses due to all but nonexistent flow of tourists and goods from the mainland Ukraine.

For the 282 thousand staff workers, almost half of which are also employed by the government sector, there are 543 thousand pensioners in Crimea. It is obvious that such a number of staff workers will never be able to provide the twice as large number of pensioners with pensions, which currently amount to 55% of the average wage. This would require a pension fund tax larger than the taxed salary itself. At the same time capping the salaries at a level sustainable for the Crimean economy would mean slashing them 2.5-3 times to an average amount of USD 79-85, roughly the level existing in today's Ukraine. But with the price tags currently observed on the peninsula this would leave the locals with a living standard 1.5 or 2 times worse than the current one in Ukraine.

Therefore pension payments (USD 1.4 billion) are possible only owing to Russian federal budget subsidies, which also being the source of generous salaries in the government sector are gradually becoming the main foundation of livelihood and employment for the local

manufacturers and services providers. The peninsula's economy has no option but to readjust to this chain of "life support": the military, the administration, state employees, and only after come those, who supply and service them. Concordantly the idea to concentrate extraordinary numbers of military in Crimea can be seen not only in the context of Putin's fixation on turning the peninsula into an "unsinkable aircraft carrier", but also as an attempt to compensate the losses from the withering flow of tourists and the curtailing of real economy at large.

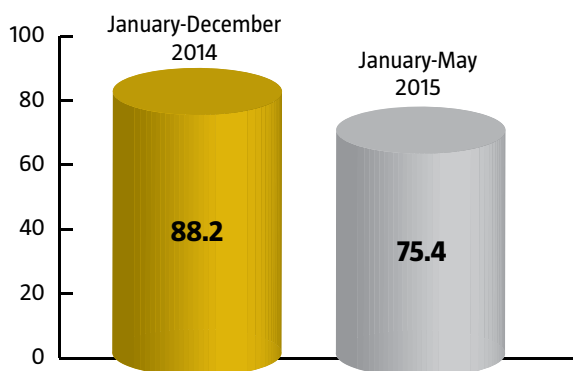
Having said that, the amount of subsidies that Crimea was promised during the annexation is constantly being revised and reduced. At first, for its support and development the peninsula was to receive almost USD 11 billion, according to the then-current exchange rate, for 2014 alone. Yet the newly amended programme approved in 2015 envisages only USD 12 billion (according to current ruble exchange rate) through 2020. Granted, a country of 140 million population and not inconsiderable (albeit halved compared to just a few years ago) oil and gas revenues theoretically can afford spending a few billion per year to subsidize Crimea. But for how long will the Russians be content with their tax money being spent to maintain the "shop window of the Russian World" in Crimea knowing that it will never achieve self-sustainability. On the contrary, the peninsula will continue drifting in the opposite direction. And what will happen to the population of Crimea itself, when the subsidy-addicted junkie faces a reduction of complete withdrawal of such backing?

BETWEEN UKRAINE AND RUSSIA

The warped social and economic reality created by the Kremlin in the occupied Crimea will make its return to Ukraine even more difficult from the financial and social standpoints. Ukraine will not be able to afford to maintain the current level of payments for the pensioners and state employees. Therefore the reintegration of Crimea into Ukraine would cause dramatic decline in the level of income (at least nominal) and growing discontent of the many current "clients" of the Russian state.

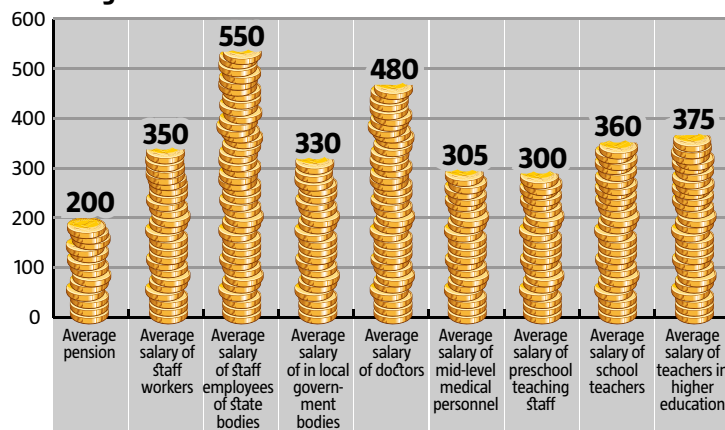
The saving grace could come in the form a transition period, when Crimea as a result of separation from Russia or its refusal to continue subsidizing the peninsula would undergo sharp reduction of payments for pensioners and state employees with these payments being adjusted to the

Dynamic of production in processing industry, % of volume in the respective period of 2013



Source: Federal State Statistics Service of the Russian Federation

Average payments to particular categories of Crimea's population, in USD according to March 2015 average official exchange rate of Russian Central Bank



Source: Federal State Statistics Service of the Russian Federation

internal capacity of the local economy. After this Crimea's reintegration into Ukraine would not lead to decrease of living standards for any category of the peninsula's population. On the contrary, it would ensure improvement for a large portion, if not the majority of the population due to falling prices and growing tourism revenues.

At the same time, the year following the annexation showed the inability of the Ukrainian authorities to ensure an effective transport and economic blockade of the peninsula. Putting it in place will become ever more difficult due to business interests of the players involved in trade with the peninsula.

Furthermore, even for Ukraine Crimea is slowly becoming one of the largest export markets. For instance, according to State Statistics Service of Ukraine, only in January through April 2015 USD 308.7 million worth of goods have been exported to what is officially called "free economic zone Crimea". This makes nearly 2.4% of all Ukrainian export. Crimean export surpassed Ukraine's export to France threefold, it was 1.5-2 times larger the export to Moldova, Romania, Czech Republic, the United States and beat Ukrainian export to Belarus (USD 243.3 million), Iran (USD 250.7 million) and Hungary (USD 282.4 million). It equaled half the export to Poland (633.9 million) and came close to the export to Germany (USD 433.8 million) and Spain (USD 356.7 million).

And the rate of Ukraine's export to Crimea is growing rapidly. For example, in the first two months (January-February) of 2015 it made USD 96.5 million, while in the next two months (March-April) it grew to USD 212.2 million. If this trend is to continue, by the end of the year Crimea may become the 4th or 5th in the list of Ukraine's biggest export markets. And considering that such goods can make their way through the occupied peninsula further into Russia proper and by doing so avoid the Moscow-imposed trade restrictions, Crimea's economy may become not only that of pensioners and the military, but also the economy of flourishing contraband and re-exportation, a place used by the Ukrainian suppliers to bypass the quotas and restrictions for Ukrainian goods that are already in place, as well those that are to be introduced in the future in response to the enactment of the economic section of the Association Agreement between Ukraine and the EU. ■

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Making Waves, If Not Ruling Them

With a mixture of bluff and opportunism, Vladimir Putin is talking up his country's diplomatic and strategic power



More than a year after America and its allies set out to punish the Kremlin for backing rebels in Ukraine and annexing Crimea, Russia is finding new friends and dealing with the West from a position of growing strength. At any rate, that is the message that Vladimir Putin has been delivering to his own people and anybody else who will listen.

In his latest flexing of muscles, the president set out a naval doctrine on July 26th which aspires to challenge the Atlantic alliance in all its areas of operation, in reply to NATO's "unacceptable" plans to move some forces close to Russia and expand its global reach. He wants an ocean-going navy, especially active in the Arctic and the Atlantic, to replace a fleet whose ageing ships mostly hug the coast.

This capped a month of diplomatic showmanship, in which the Russian city of Ufa, on the boundary between Europe and Asia, hosted summits of two organisations which aspire to challenge America's

global leadership. One is a mainly economic club known as the BRICS (including Brazil, India, China and South Africa); the other is the Shanghai Co-operation Organisation (SCO), focused on defence, which includes China and the ex-Soviet republics of Central Asia and has just gathered in both India and Pakistan.

As Russia's state media told the story, the BRICS meeting was a new step in the construction of a counter-weight to the Western financial system; it established a \$100 billion currency reserve fund which would emulate the IMF's role as a stabiliser of monetary crises, and confirmed plans for a \$100 billion development bank. The clear message was that, despite being excluded from Western capital markets, Russia has alternative economic partners.

In the tart words of Andrei Klimov, deputy head of the Federation Council's foreign relations committee: "When a person turns his back on you, you have two choices—you can run after that person, or you can start to talk to other people."

Meanwhile the sealing on July 14th of a nuclear deal between Iran and six world powers, led by America but including Russia, allowed the Kremlin to argue that the West still needs it. When Barack Obama thanked Mr. Putin for his help with the accord, this seemed to boost the hope of some Russian officials that the West might give ground over Ukraine, or elsewhere in eastern Europe, because it craves Russian help in places like Iran or Syria.

In a quieter display of soft power, Mr. Putin's advocacy of "traditional values" got a fillip on July 3rd when, at the UN Human Rights Council, a motion lauding the conventional family was carried by a clear majority, led by Russia and Islamic states, against opposition from America and western Europe, which wanted a mention of new realities like gay partnerships.

Alexei Pushkov, who chairs the Duma's foreign-affairs committee, sees in the American Supreme Court ruling establishing gay marriage one more chance for Russian-led pushback. America will try and fail to propagate such unions, he says.

But behind all the self-confident talk, over economics, defence or values, how well is Russia resisting Western pressure? In the cold light of day, Mr. Putin's rhetoric looks like a mixture of vain boasts and calculated realism.

Above all, China seems unlikely to meet Russia's hopes, either as a provider of capital or as a security partner. Its economy towers over Russia's and it does not share Mr. Putin's keenness to pick fights with the West. According to Angela Stent, a professor at America's Georgetown University, most of the economic benefits from Sino-Russian co-operation are still far off. Talks on a pipeline taking Russian gas to China foundered this week. In China plans for an Asian Infrastructure Investment Bank, a development body that excludes America, takes priority over any BRICS project.

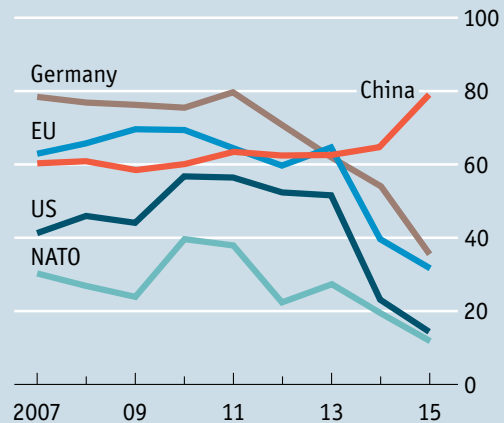
Nor is the SCO about to become a close-knit club comparable to NATO. Although China buys Russian weapons, the countries have their differences over security; for example, China resents Russia's enduring ties with Vietnam. And Russia's expansionism in Ukraine has made other neighbours, like Kazakhstan, more wary.

The Iran accord is also a mixed blessing for Russia. As Fyodor Lukyanov, editor of the journal *Russia in Global Affairs*, points out, Russia resisted economic sanctions against Iran (while going along with them in deference to its Western partners) so it should logically gain from their removal. But the deal could hurt Russia by lowering world oil prices and bringing new gas supplies to Europe; and under the letter of the deal, Russia will not be able to sell arms to Iran, as it badly wants to do, for at least five years. The real prize for Russia could come from unhappiness over the deal in Saudi Arabia, which is annoyed with America and looking for fresh financial partners.

Of all Russia's initiatives, it is the naval expansion, part of a big drive to rearm that seems immune to budget cuts, that will be studied most in Western capitals. Russian yards have lost the capacity to build big surface ships, especially without access to parts from Ukraine. Its sole aircraft carrier is 30 years old and hardly seaworthy. It will be lucky if, as proposed, a new one can be launched towards 2030.

We know what we don't like

Percentage of Russian respondents with favourable views towards:



Source: Pew Research Centre

But Russia has always been able to make stealthy, deadly submarines, and it seems to have solved some problems with new types of conventional and nuclear-capable subs. Three of the latest sort of nuclear-armed boat are now plunging the ocean's depths; seven more are planned. Although America's navy, which soon aims to exceed 300 large ships, dwarfs all others, Russia's naval effort is serious. The new doctrine implies eventually being able to confront NATO in every ocean where Western navies sail, albeit in ways short of war, says Peter Roberts, a research fellow at the Royal United Services Institute, a think-tank in London.

With its economy crimped—more than it admits—by Western sanctions, Russia's best hope of fulfilling

VLADIMIR PUTIN SET OUT A NAVAL DOCTRINE ON JULY 26th WHICH ASPIRES TO CHALLENGE THE ATLANTIC ALLIANCE IN ALL ITS AREAS OF OPERATION, IN REPLY TO NATO'S "UNACCEPTABLE" PLANS TO MOVE SOME FORCES CLOSE TO RUSSIA AND EXPAND ITS GLOBAL REACH

such a plan lies in persuading citizens to tighten their belts for the sake of a nation that supposedly faces a perpetual American peril. For Anna Glazova, of the Kremlin-linked Institute of Strategic Research, there is ample evidence of such a threat: proof positive is provided by the fact that Mr. Obama once mentioned Russian misbehaviour, the Ebola virus and Islamic State terror all in the same speech.

For anyone who recalls Soviet times, this mix of defensiveness and defiance feels familiar. And in case proof were needed of Russia's determination to say *nyet*, it vetoed, on July 29th, a UN security council resolution to create a tribunal to probe last year's downing of a Malaysian airliner over rebel territory in Ukraine. ■

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Steven Pifer:

“I don’t see any significant change in the American policy about Ukraine because of the Iran issue”

Interviewed
by
**Anna
Korbut**

The *Ukrainian Week* spoke to the former US Ambassador to Ukraine and currently Director at the Brookings’ Arms Control and Non-Proliferation Initiative about possible changes in America’s policy over Ukraine and Russia after the Iran deal, and about expectations for the Minsk process.

The U.S. deal with Iran, followed by news of Vladimir Putin’s call to Barack Obama and Obama’s praise of Russia’s role in the process, sparked speculations about possible change in America’s course on Russia over Ukraine as well. Do you see any links between these aspects?

That kind of connection between Ukraine and Iran is dramatically overstated. Russia cooperated with the US, the EU and China during the Iran negotiations, because it was in Russia’s interest not to see Iran with nuclear weapons. Russia’s relations with China also were probably a factor that encouraged Russia to make sure the deal would not derail.

I don’t see any significant change in the American policy about Ukraine because of the Iran issue. Washington policymakers are perfectly capable of compartmentalizing diplomacy. They can have significant differences with Russia over Ukraine, but at the same time there are issues where America’s and Russia’s interests converge and where the two can cooperate. Iran was one of them.

When I was posted at the American Embassy in Moscow in 1987, we almost had completed the Intermediate-Range Nuclear Forces Treaty, and we were making progress on strategic arms as well as on some human rights issues. At the same time, the US was sending Stinger missiles into Afghanistan to target the Soviet army. Washington and Moscow know how to compartmentalize issues.

Another disturbing case was Victoria Nuland’s visit to Kyiv to push through amendments to the Constitution which many in Ukraine see as controversial and dangerous for the country’s territorial integrity. Now, that Ukraine has made this step forward in implementing Minsk-II, while the US and the EU have no leverage to push the other side take their steps, and the tentative deadline for fulfillment of Minsk is set for the end of 2015, will the US and European allies be willing to push Ukraine further into concessions?

I would make three points here. First of all, if you look at what the American and European governments are saying, they are much more critical about Russia and the separatists in terms of compliance with Minsk-II. It is Russia that is under Western sanctions.

The second point, there is a view in the West that the Ukrainian government’s position will be stronger

politically if Ukraine can make the “we are doing everything we can to stick to Minsk-II” argument. Then the compliance problem is entirely on the Russian and the separatist side.

The third point. Quite apart from the issue of the Donbas and separatists, the American government seems to favor decentralization in general. I agree with this. The Ukrainian government, as it is structured today, has too much authority and power in Kyiv. It is more efficient and more effective to push some decision-making down to regional and municipal levels. That is a reform the American government would encourage Ukraine to take even if it didn’t have the current situation in eastern Ukraine.

Decentralization, however, does not mean delegating authority on national-level decisions like defense policy or foreign policy to regional or local authorities. What it means is pushing down authority on issues like education and healthcare.

This does sound right in theory. However, Ukraine has been centralized de jure, as well as financially, while de facto regions have been a sort of fiefdoms of local oligarchs, political clans or top officials who had leverage to influence courts, prosecutors and police. Zakarpattia and Odesa are the most telling examples of how this has been working. This leads to a concern that decentralization without properly functioning institutional base will only reinforce local landlords. Is that factor understood or considered?

I understand that concern. But I would also ask a question – is the current system with so much authority in Kyiv effective? What Ukraine needs to do is move to a system where, for example, the regional governor is directly elected so the voters have an ability to vote that person out if he or she is corrupt. That is more likely to enable people at the regional and local levels to replace officials they believe are corrupt or who are pursuing policies the voters disagree with.

According to Minsk-II, the next step after decentralization is elections in the occupied parts of Donetsk and Luhansk oblasts, followed by the sealing of the border. However, given the fact that any dissent has met violent persecution in those areas and many people, including pro-Ukrainian ones, have fled, do Ukraine’s foreign partners see a possibility of decent elections there? And if that doesn’t happen by the end of 2015, are any backup plans discussed?

If the so-called Donetsk and Luhansk People’s Republics allow the OSCE to assist in organizing and holding an election that is closely monitored, the possibility of decent elections could be there. Unfortunately, I don’t see the separatists prepared to allow

that. But it strengthens Ukraine's position internationally if Ukraine says that it wants to work with the OSCE in holding the elections in the occupied parts of the Donbas that are free and allow the voters to express their views.

As for backup plans, my impression is that right now Western leaders are holding on to Minsk-II although they realize that it is not being implemented well. However, that is the only deal on the table that has been agreed by the Ukrainians, the Russians and the separatists.

It is important for Ukraine to position itself as a party that has done everything possible to implement Minsk-II. If we come to the end of the year and the agreement is clearly not completed, which is my expectation unfortunately, Ukraine wants to be in a position where all the blame for the failure to implement Minsk-II lands on the separatists and Moscow. Hearing people like Zakharchenko say that "we will never allow Ukraine to reestablish control or sovereignty", when a principal aim of Minsk-II was to allow Ukraine to reestablish sovereignty over all of that region, doesn't help the separatist side. It is the separatists who do things contradictory to the agreement. When December 31, 2015, comes and it becomes clear that Minsk-II was not fulfilled, Ukraine should seek to be in a position where all international blame goes to the separatists and Russia.

With the latest constitutional concessions that should contribute to Ukraine's position internationally, but the slack pace of reforms, do you see any weariness over Ukraine and its prospects developing amongst American policymakers?

I wouldn't say that. The sense here in Washington is that Ukraine has an opportunity. Doing reforms is hard, but the more that is done and the more quickly it is done, the shorter the period of economic pain.

Meanwhile, high-level consultations between the US and Ukraine are active. US Vice President Biden has been to Ukraine three times over the past year. Ukrainian President Poroshenko and Premier Yatseniuk have both been to the US. There are regular phone calls between the leaders. Diplomatic relations look like they are in a pretty good shape.

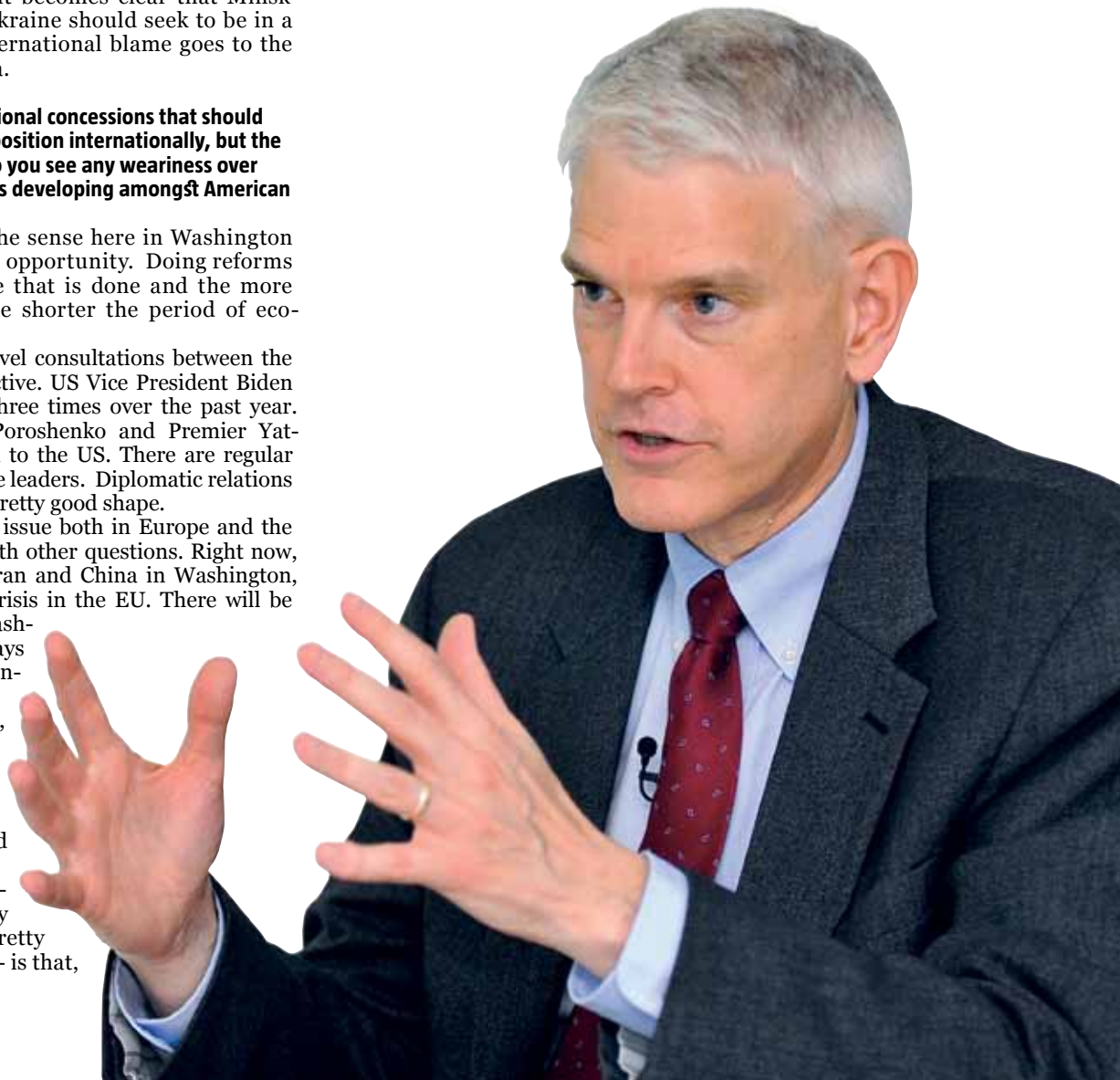
Ukraine is a major issue both in Europe and the US, but it competes with other questions. Right now, it is competing with Iran and China in Washington, and with the Greece crisis in the EU. There will be much attention in Washington in the coming days and weeks as the Congress will vote on the Iran deal. Hopefully, Europe will deal with Greece and, as these issues are settled, that will allow the West to think in a more focused way about Ukraine.

What is interesting, however - and my guess is that it was pretty disturbing to Moscow - is that,

with all of the EU's attention on Greece, it decided to extend sanctions on Russia in June from July 2015 till the end of January 2016 at the technical level. There wasn't even a debate on the senior political level about that. So, the default mode for the EU was to sustain the sanctions. If there is a major separatist attack - on Avdiivka or Mariupol - my guess is that the West would apply additional sanc-

"DECENTRALIZATION DOES NOT MEAN DELEGATING AUTHORITY ON NATIONAL-LEVEL DECISIONS LIKE DEFENSE POLICY OR FOREIGN POLICY TO REGIONAL OR LOCAL AUTHORITIES"

tions on Russia. And there is still some distance for the West to move with sanctions: the current sanctions are at around a level of 3-4 on a scale of 1 to 10, so a lot more can be done. I hope that there will be more serious consideration of additional sanctions in case Russia has made no real efforts to implement Minsk-II by the end of the year. ■



The Force of Habit

Alla Lazareva, Paris

The interests and prejudices of officials and diplomats from the UN, OSCE, Council of Europe and other international agencies sometimes affect policy decisions more than they should

"People are always more important than the institutions they work for," the former French Ambassador Philippe de Surenin likes to remind everybody. The truth of these words is confirmed every time we see how truly limited is the influence of international agencies on events in the planet's hot spots. The post-war checks and principles for decision-making ensure that they have a very tiny arsenal indeed: declarations, reports, observers' missions, "concern" and "indignation"...

The UN Security Council is paralyzed by the prospect of a Russian veto, the OSCE and Ministerial Committee of the Council of Europe—by the mandatory principle of consensus. Moscow—or, hypothetically, any other member that is not interested in serious steps being taken against it—can easily avoid them. Might makes right is, of course, a medieval principle, yet recent developments in Donbas and Crimea testify that this principle has not outlived its time at all. On the contrary, it works quite well, thank you, in the Minsk accords. This document does not even state what should happen, if one of the parties deliberately ignores the agreement. So what next? In an ideal world, those in violation should find themselves facing serious obstructions. In reality, pressure continues to be put on Ukraine, simply because that's much easier to do. And whatever cannot be really brought to bear against the DNR militants or on Russia, the OSCE mission simply spreads its hands and says, "We don't have access to 40% of the occupied territory. Sorry. We do what we can. And what we can, compared to the scope of the challenge, is not much at all."

"Unless the OSCE is stationed all along the ceasefire line, is stationed in Shyrokyne with all the necessary technology and as many observers as is possible, and—let's call it like it is—stands there on a permanent basis, there's no way that the ceasefire will ever be stable," Foreign Minister Pavlo Klimkin told Channel 5 in a recent interview. "We need the OSCE to completely control the withdrawal of all weaponry. They are ready to monitor this, but they simply aren't being given access. But if the OSCE were to really stand all along the ceasefire line, our boys would stop dying from the endless shelling."

Yes, indeed. If the OSCE were to line up along the nominal boundary between occupied and unoccupied territories, things would definitely be a lot simpler. So how do we get there from here? "In the last 24 hours, the terrorists violated the ceasefire 95 times," is what we hear on every day from various news sources. Every day, Ukrainians are killed or wounded and the shelling just doesn't stop. And so? Nothing. Russia pays for 7% of the OSCE's budget and that gives it the right to have 7% of its own observers in any mission—and that's not all. If it so chooses, the Russian Federation can nip any undesired



Abstract diplomacy. OSCE Secretary General Lamberto Zannier mentioned only "militias wearing no identification" after a visit to Ukraine

initiative in the bud because Council of Ministers decisions, according to the OSCE charter, must be approved unanimously.

"It's important to understand that international organizations are not institutions that exist and develop on the basis of defending specific principles," Bohdan Yaremenko, diplomat and chair of the board of the Maidan of Foreign Affairs, told *The Ukrainian Week* recently. "The main role in any international organization is played by national governments. In fact, any international organization is founded on the interests and activities of governments. They may announce that they are dedicated to some principles or ideals and have decided to set up this entity in the joint defense, promotion or development of said principles. But the positions of individual governments change and the organization has to then either recognize that one of its members has stopped acting honestly and responsibly or try and close its eyes to the obvious."

"Theoretically, all the countries that are members of international organizations and unions—with the exception of the Customs Union—are equal. And so, when it comes to voting, Russia's influence is not only equal to France's, but also to Ukraine's. Informally, everything depends on the level of professionalism, motivation, organization and resources of each individual national delegation or national diplomatic corps. In fact, only a few countries can globally control the agenda in organizations like the OSCE, the UN or even the Council of Europe."

Mr. Yaremenko went on to explain: “To globally control means to take active, conscious participation in reviewing each and every issue that is on the organization’s agenda. Most countries monitor a limited range of issues and do not react at all to the rest that, in their opinion, do not affect their own interests. This offers advantages to those who operate on a global, mass and systemic level.”

For many subjective and objective reasons, Ukraine is not one of the players in this global group. “Ukraine’s diplomats exist and function to the same extent as, say, its judiciary or education or healthcare systems do,” Mr. Yaremenko said. “In other words, there is an agency, there are powers and people. But it only creates the illusion of goal-oriented, effective activities. In 18 months of war, there has been not one initiative, not one draft propose or fresh idea from Ukraine’s diplomats. Not one achievement other than a completely unintelligent campaign that repeats that Russia is bad and there is no alternative to the Minsk agreements. This last is really telling: Ukraine’s diplomats see no alternative to negotiating with a state that they do not trust at all.”

Indeed, the Minsk accords are the inevitable result of “reactive diplomacy,” which is mostly what Ukraine seems to practice. A year ago, the world agreed to a format of negotiations with Russia regarding its attack on Ukraine’s lands. This was the Geneva format and it was the most beneficial to Ukraine, following the formula, US–EU–UA–RU.

But, as one diplomat put it, “Nobody would have agreed to rescue Ukraine in a format that did not suit Kyiv. Yet Kyiv showed no initiative whatsoever while Moscow did everything within its power to prevent the US and Brussels from participating.” And so, instead of the Geneva formula, Ukraine ended up with the Norman one: France, Germany, Ukraine and Russia. With the Minsk “codicil” that allowed for “consultations” with terrorists. Moscow takes hissy fits; Kyiv genteelly holds its tongue. And that’s how it is.

Is it fair to say that it’s all about the effectiveness of the pro-Russian lobby in the virtual absence of a pro-Ukrainian one? In the habits and prejudice of western politicians? It’s a bit of both.

“You have to understand that, for us, Ukraine is like a Russian Gabon,” a French official admitted off the record. “We understand Russians because we also ensure a local government that suits our interests in our former colonies and gives us access to the resources we need. These spheres of influence were not formed yesterday and they won’t disappear tomorrow.”

The heads of top international organizations rarely surprise us with clear assessments of what is going on in eastern Ukraine today. For instance, the OSCE Secretary-General, Italian Lamberto Zannier visited the frontline zone twice. He was in Dnipropetrovsk and spoke with the members of the mission currently working in the Donbas. What were his conclusions after both trips? “OSCE mission experts did not see any individuals without identifying marks crossing the border even once,” he told a UNIAN correspondent. “This is a very strange situation, because we see many different people and we cannot say who they are, what their orders are, and why they are doing what they are doing. We don’t know if they are motivated by ideology or are organized according to some other principle. And this makes it much more difficult for us to understand what’s going on.”

This is the language of Aesop: We understand everything but we say almost nothing. Should we call a spade a spade? If we don’t have to, why bother?

The UN, where Russia has blocked an international tribunal in the MH17 case, isn’t much better. “We joined forces with the United States, Great Britain, the Netherlands and Malaysia,” a Ukrainian diplomat told *The Ukrainian Week*. “Obviously, these countries are interested, not so much in helping us as in helping themselves, but this offers Ukraine the only ghost of a chance to achieve some kind of process. Yes, it would be somewhat in someone else’s hill, but we need to get to this peak. We can’t do it on our own, because we don’t have the resources, the political will or the support.”

In the Council of Europe, we can see the same alignment of forces. A year ago, in violation of the sanctions and at the invitation of the president of PACE, the Speaker of the Russian Duma, Sergei Naryshkin visited France. “These consultations were necessary to find a way out of the crisis at last,” Liberal Anne Brasseur and PACE’s top official defended her position when challenged by journalists. But no way out was actually found, while the controversial invitation only made it clearer that the Council’s stated principles could be bent through pressure from various Kremlin agents and the personal influence of Thierry Mariani, the member of PACE’s French delegation who organized Naryshkin’s visit. Such examples are rife.

“The greater the role of individuals, the worse the system works,” says Bohdan Yaremenko. “A strong personality can impose their will on an organization. But then we have to ask, what exorbitant price are we willing to pay for possible mistakes and the growing likelihood that this individual will prove wrong? But when the system is falling apart, unintellectual, poorly managed, corroded by conformity and corruption, then there may be no other way to move forward, other than through the will of strong individuals.”

That is the way of this world. Imperfect and insecure, where justice is only an ideal to which we aspire.

In the current context, state diplomacy has ever shown itself to be more effective than the limited and clumsy diplomacy of international organizations. The

THE SYSTEM OF INTERNATIONAL COORDINATION OF POLICY IS WEAK AND POROUS AND ILL-WILLED, OVERWEENING AMBITIONS EASILY FLOURISH IN IT, AS WE HAVE SEEN HAPPEN WITH RUSSIA

legitimacy of actions in these situations is far less and the personal responsibility of leaders many times greater. And yet, it offers the chance to control the game. Reforming international institutions risks a second possible conflict, although something is being done in this area. But real changes will, at best, materialize only a few years down the line.

The system of international coordination of policy is weak and porous and ill-willed, overweening ambitions easily flourish in it, as we have seen happen with Russia. The challenge of our times is to find restraining mechanisms to counterbalance the entrenched habit of dividing the world into “spheres of influence.” It’s entirely possible that this is where Ukraine’s historical mission lies. ■

Michael Bociurkiw:

“We are able to be the eyes and ears of the international community in the conflict area”

Interviewed
by
**Anna
Korbut**

The Special Monitoring Mission is one of the OSCE's numerous missions. It is tasked with collecting information, establishing facts and reporting on the security and human rights situation on the ground. Under its mandate, the SMM does not conduct investigations or draw conclusions. Moreover, the monitors are unarmed civilians protected only by armored cars and personal protective equipment. Given security considerations, they are unable to work under shelling. Therefore, some may get an impression when reading their reports that the documents do not reflect the situation on the ground in Eastern Ukraine completely because, for example, they do not point at the side that starts the shelling. *The Ukrainian Week* spoke to Michael Bociurkiw, the Spokesperson of the OSCE SMM, about its mandate and tasks in Ukraine.

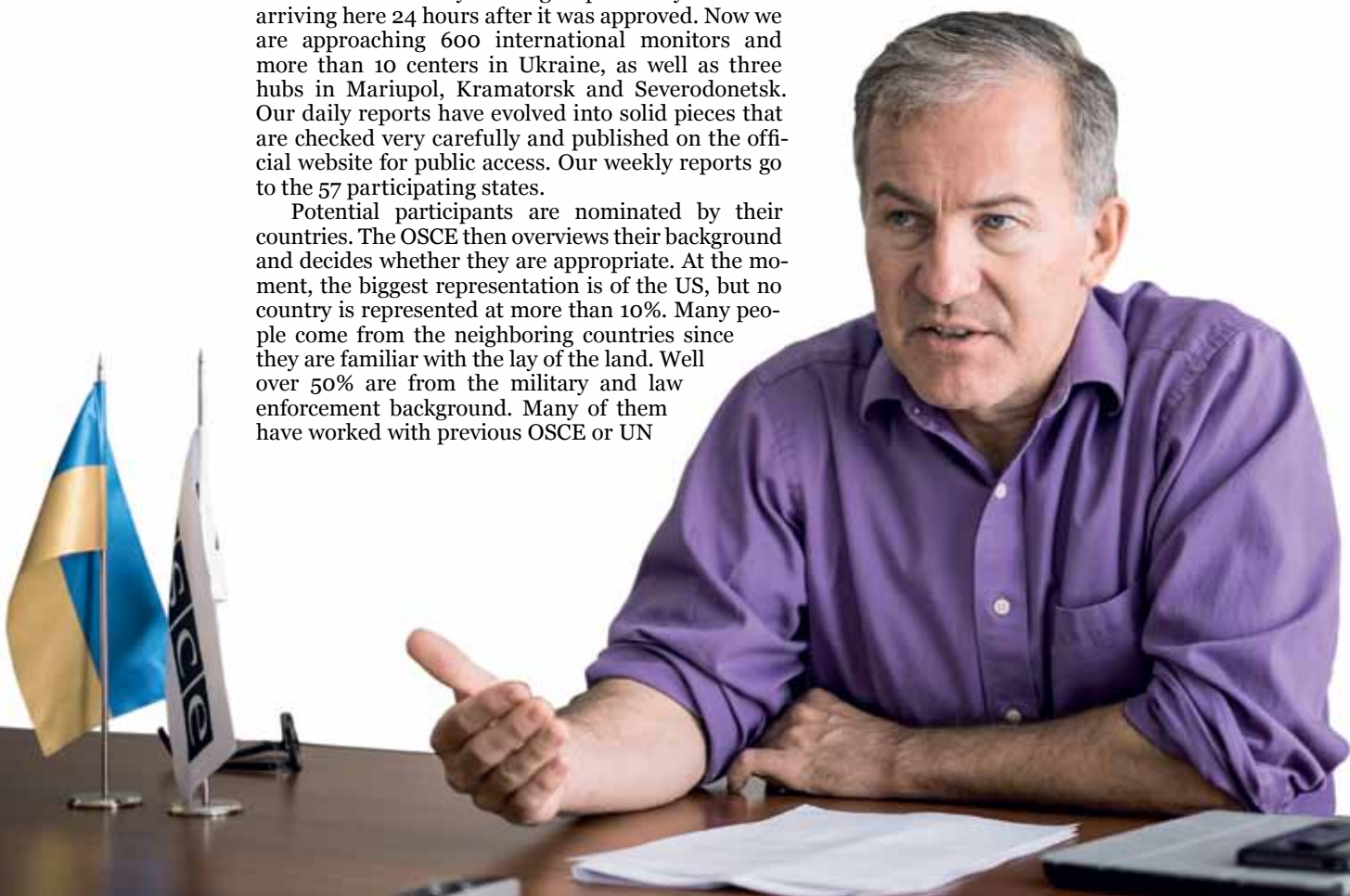
What criteria have been used to select monitors for Ukraine? And what are the proportions of member-state representatives in the SMM?

The mission—a very small group initially - started arriving here 24 hours after it was approved. Now we are approaching 600 international monitors and more than 10 centers in Ukraine, as well as three hubs in Mariupol, Kramatorsk and Severodonetsk. Our daily reports have evolved into solid pieces that are checked very carefully and published on the official website for public access. Our weekly reports go to the 57 participating states.

Potential participants are nominated by their countries. The OSCE then overviews their background and decides whether they are appropriate. At the moment, the biggest representation is of the US, but no country is represented at more than 10%. Many people come from the neighboring countries since they are familiar with the lay of the land. Well over 50% are from the military and law enforcement background. Many of them have worked with previous OSCE or UN

missions, are familiar with the region and speak Russian. Many have particular expertise in crater analysis which is necessary to determine the direction from which the shelling comes from. We also have human rights, media and dialogue facilitation experts. They work in teams—the patrolling group usually numbers from four to eight people. Now, two thirds of our monitors are in Eastern Ukraine because of the tense situation.

We are often asked why we have so many Russian monitors. But their number is 26 out of 516 international monitors, which is 5%. It is important for us to have Russian-speakers and people who understand the local cultural background. These monitors have had quite a bit of experience in the region in previous missions. Importantly, everyone who comes here as part of the mission and OSCE, signs the Code of Conduct. All of the information the monitors collect and sent to Kyiv is double- and triple checked before being published in our daily reports.



The SMM is often criticized for ineffectiveness of its monitoring or not being present during dangerous episodes — at night, for example — or for arriving during ceasefires while the shelling resumes once the group leaves. How accurate is this? Does this approach affect the quality of your reporting?

We've heard that criticism. For one thing, we do not patrol at night because it is too dangerous. Regarding the observation about the shelling resuming when a monitor group leaves: not long ago, our monitors were pinned down for 90 minutes while the shelling was happening. And that occurs with increasing frequency. However, we are a civilian mission and we are unequipped to have fire pointed at us. Recently, one of our team members was injured in Shyrokyne. That shows you that we are very close to the action and we report when we see the shelling happening.

We are now more concerned because heavy weapons such as GRADs and multiple rocket launch systems have been reintroduced into the theatre. Though many weeks after Minsk, we shouldn't be in this position. There should be calm, withdrawal of heavy weapons and moving away from the contact line.

More widely, there are very high expectations for the SMM. We try to explain to people why we are here and what we are doing. It is important to understand that we are here upon invitation of Ukrainian government. They are the ones who asked the extension of our mandate.

Meanwhile, most people see the mission in the middle of all of this and think that it can bring about peace. However, it is up to the sides to have political will to bring about calm. We can report on what we are seeing and on human rights violations, help facilitate dialogue and reduce tensions. We have already launched radio spots to better explain to people why we are there.

But we have noticed that people's frustration has grown, especially in the conflict zone. The locals are tired, they want the shelling to stop. Hundreds of IDPs we have talked to told us that what will take them to return home is for the shelling to stop. There is concern that the longer the displaced people stay where they are, the more difficult it will be for them to go back.

Another aspect that we have been reporting on is the unbelievable damage to the civilian infrastructure—roads, bridges, hospitals and schools. Those have been severely shelled. The repair bill will be huge. We are also starting to take concrete steps towards facilitating demining that would enable us to go to places like Shyrokyne.

How often does the SMM face restrictions to the sites it has to monitor?

Sometimes, we are physically unable to go to a certain place. For example, we were unable to go

Michael Bociurkiw is Canadian journalist. He has reported for *Globe and Mail* and *South China Morning Post*. Mr. Bociurkiw is currently Speaker of the OSCE Special Monitoring Mission to Ukraine. Before this, he was Speaker for various UN missions, including UNICEF in East Jerusalem

to Shyrokyne because of the danger there. At times, we are delayed at checkpoints on both sides; they have procedures for documentation and want to search our vehicles. We have also been prevented from accessing heavy weapons storage areas or have been allowed to the areas but were restricted in what we were allowed to do—for example, checking serial numbers on heavy equipment. That is unacceptable. We need free, safe and unfettered access to do our job, and we rely on both sides for that. If we don't have that access, we report on this and identify the parties that restrict access for us, as well remind them as often as we can about our mandate and why we are here.

As of today, both sides have yet to provide us with the full inventories? on what heavy weapons they actually have and with the routes they will use to transfer heavy weapons, so that we can monitor them. Also, they have to tell us where they are going to store those heavy weapons so that we could go and monitor. We have made several appeals to do that. Some heavy weaponry has been removed. But we are not here to report on the movement. What we want is to certify and verify that heavy weapons have been moved away. We don't have that possibility yet.

More generally, the value of the reporting is that we are able to be the eyes and ears of the international community in the conflict area and report on specific incidents, the impact on the civilian population. People who have stayed in the East are having a very difficult time with everything from sending their children to school to getting medicines, essential goods and pensions paid, as well as with the Ukrainian-imposed permit system. It has shown the difficulties people are having with it—things like bureaucratic delays. We do report on that. Another important aspect of our work is facilitating dialogue and access. For example, when MH17 came down, we were on the ground there 24 hours later, reporting to the world on what was going on, and facilitating access for experts and emergency workers. A couple of past weeks we've been busy in places around Horlivka facilitating access for workers to repair water pipes damaged from the shelling. Not only does this restore infrastructure, but it shows that the two sides can actually agree to put down arms for a few hours at least every day, and it is possible for calm to happen.

At the end of the day, we establish facts. We report as much as we can, based on what we actually hear and see. For example, if there was shelling in Shyrokyne and the situation allows, we will go there and observe what is going on, and report as much as possible on where it comes from. But we are not pointing fingers: there is enough information in our reports to enable people in the relevant positions to take action if need be. ■

Representatives of OSCE member-states in the SMM to Ukraine as of July 29, 2015

USA	Romania	Russia, Poland and Finland, each	Hungary	Germany	Italy	UK and Sweden, each
50	30	26	23	22	21	18

Total of **516** people from over **40** OSCE member-states

Hanna Hopko:

“Western partners often do not understand what Ukraine wants”

The *Ukrainian Week* spoke with Head of the Verkhovna Rada Committee on Foreign Affairs Hanna Hopko about Ukraine's cooperation with Western partners and international organizations, the consequences of the Minsk agreement and the upcoming local elections.

Do you consider the Minsk format effective in the current crisis? Can there be an alternative?

The Minsk agreements are basically a forced step Kyiv had to take under pressure of the Russian military offensive and the state of the Ukrainian economy. Starting with the Minsk agreement signed in September 2014 steps were taken that allowed to stabilize the front line, reduced the intensity of military actions and loss of human lives and gave us the possibility to cut costs and gain time to prepare to win this war.

Compared to a year ago, the Ukrainian military has made notable progress in terms of staffing and armament. But we are not ready for full-blown invasion as the price would be human lives. For this reason we are exploiting the Minsk process, though we are not happy with it. It is important to understand how additional strategies to defend our interests can be built through and around the Minsk agreement. By conducting reforms and fighting corruption, we are sending out a message to Russian citizens that under Russian aggression Ukrainians are becoming stronger, and to the international community that is providing us with financial and humanitarian aid.

The state must be built in unity, people must play as a united team where every member has an own role. It is critically important that the interests of the state prevail over the interests of financial groups or political factions. What some parliamentarians are doing is not permissible. They cry out “We do not recognize the Minsk agreement!”, but they do not propose alternatives. If we speak about alternatives – whether we should expand the circle of our allies, increase the number of negotiating parties or strategic partners – this must be discussed.

I recently received from the U.S. Vice President Joe Biden a positive response to my letter requesting expansion of sanctions against Russia, including expulsion from SWIFT, should Russia fail to fulfill its urgent commitments under the Minsk agreement. The United States are not officially part of the Normandy format, but they are involved in negotiations and the official visits of John Kerry, Victoria Nuland and Joe Biden to Ukraine are testimony to the fact that the U.S. is actively participating in counteraction to Russian aggression.

For Ukraine, this opens the possibility of close cooperation with the entire world – Australia, Japan, African nations and the Arab world. When export to Russia is blocked, it is time to seek new export destinations for

Interviewed
by
**Vitaliy
Rybak**

our goods. The lifting of sanctions against Iran opens an additional source of energy for Europe and weakens the influence of Russia on the global market. The situation is rapidly changing, which is why we must have a sober understanding of challenges and opportunities.

Is the Ukrainian leadership facing pressure from Western partners to speed up decentralization and reforms in general?

Saying something like “you’re being pushed into doing something” only plays into Russia’s hands. The Kremlin wants to disband the parliamentary coalition by fueling disputes about constitutional reform. Many messages will be spread to fuel squabbles amongst those who have not looked into it in detail.



PHOTO: UNIAN

Hanna Hopko, born in 1982 in Lviv Oblast, was educated as a journalist and holds a PhD in communications. She worked on television and radio, volunteered and worked at NGOs. Ms. Hopko is on the coordination board of the Reanimation Package of Reform, and head of the Verkhovna Rada Committee on Foreign Affairs since December 4, 2014.

Western partners often cannot understand what Ukraine wants – we cannot afford to confuse them. Politicians should not cry out that somebody is putting pressure on them. Instead, they should effectively fulfill their obligations by cleaning the Augean stables in the Ministry of Defense, the defense industry, agribusiness and industry. Everyone must play their role. It's as simple as that. We have several tasks at hand: resistance to Russian aggression, winning international support in different sectors and developing information campaigns.

The U.S. Embassy in Ukraine is supporting public service broadcasting so that we finally have a quality product with professionally made content that Ukrainians will want to watch. This could encourage people to think more critically and compete with TV channels controlled by oligarchs. We must understand how to exploit the support of the West: we should request actual assistance to restore Eastern Ukraine rather than more loans. As far as loans are concerned, we must be responsible and spend them effectively.

Unity is the key resource for Ukraine. Thanks to unity Turkey managed to double its GDP and become a regional leader with huge ambitions and actual influence. This is because it clearly understood that this in the country's best interests. Ukraine must take this as an example. I encourage Ukrainians to pursue sound pragmatism, adequate judgment and understanding of our strategic interests.

The decentralization amendments passed by the Verkhovna Rada recently expand the powers of local communities. This makes the upcoming local elections in October all the more important. How do our Western partners see the process of elections in occupied territories? How can transparency be guaranteed there?

This year we have conducted budget decentralization – now local councils have more funds, but they often do not know how to spend them, as they do not have a far-sighted strategy. And what is the priority for cities: building roads, investing in hospitals or opening new schools? This requires a concrete program: the community should assemble and stop pointing at what the president, the parliament or the government has to do for it. From now on, you and your mayor are responsible for the future of your city. Then, having greater financial wherewithal, local politician will bear greater responsibility, because if something goes awry local residents will hold them to account, not Kyiv. The move will boost effectiveness, and the argument that the “upper echelon is in the way” will no longer be valid. People should be able to take care of themselves.

Unfortunately, in many regions there are no realistically worthy cadres to run in these elections and assume responsibility. We will hold these elections, and they will reboot local elites, even if only partially. Under the new Constitution, the next elections will be held in two years (after the ones in October 2015 – Ed.). This will be a good new opportunity.

Voters will see their elected candidates in action and realize whom they want to see running their constituency. In addition to that, this presents an opportunity for international and Ukrainian NGOs to prepare cadres. I know that the International Republican Institute supported by Canada will conduct studies for mayors and their teams, deputies and activists.

We and our Western partners understand this perfectly well and the parliament did the right thing by amending the Law “On a Special Procedure of Local Self-Government in Some Parts of Donetsk and Luhansk Oblasts” to outline nine clauses on how the elections should be held in those regions. These will not be sham elections as Ukrainian parties and politicians will participate while OSCE and other international observers will monitor, but this should not be done at the terrorists' gunpoint.

Ukrainian media should be present during these elections, but only after heavy weaponry is withdrawn and when the terrorists are disarmed. Also, we must rely on the voters' responsibility – the race in Chernihiv showed that this can be problematic. Voters must understand that when they vote for a politician, they are responsible for their vote. This is mutual responsibility of both the voters and the politicians they elect. They should actively interact after the elections as well.

At the moment, we are observing a very worrisome trend of complete desacralization of power. Some are fueling a pessimistic sentiment that there are no hon-

“WE HAVE UNIQUE OPPORTUNITIES TO INTEGRATE INTO INTERNATIONAL ORGANIZATIONS, BUT WE NEED A SOUND STRATEGY TO DO SO”

est politicians and that they are all bad. This crushes belief that some politicians actually do work for the benefit of the state.

How effectively are international organizations working in Eastern Ukraine? For example, the OSCE: to what degree does their mandate enable them to facilitate the resolution of the conflict?

On the one hand, we understand that the effectiveness of the OSCE must be enhanced. They themselves understand this too. Recently in Helsinki at the 40th anniversary of the Helsinki Final Act it was stated that the OSCE must be reformed so as to be able to prevent conflicts.

On the other hand, if we are very critical of the OSCE with not alternatives, we will push ourselves into a situation where our laments bring about zero result. We criticize them, and then talk about demilitarization of Shyrokyne and the need to increase the presence of the OSCE.

In all talks with EU member states, Canada and others we ask for the support of the UN and its peacekeeping mission. In addition to that we need to increase the presence of the OSCE and those organizations that are providing us assistance – the Czech organization People in Need and the Red Cross. We must clearly realize that there are no better options for the current tasks.

At the moment, we have unique opportunities to integrate into international organizations, but we need a sound strategy to do so. Participation in international organizations and their presence in the East is a great learning opportunity. We must find strategic partners but not brag about it everywhere. There should be a group of people who have a clear vision of Ukraine's future domestic and foreign policy, and who are ready to sit down with the Western partners, think about it and implement it together. ■

Working on the Ground

Stanislav Kozliuk, Severodonetsk

Initially, local civilians and the military had been quite critical of the OSCE monitors. This has changed recently



A new trend: OSCE monitors are now seen more often in the frontline towns and villages than

As the war broke out, Severodonetsk became to host the authorities that fled the occupied part of Luhansk Oblast, as well as the team of international observers assigned to monitor the conflict in Donbas and register violations of the Minsk agreement. The author of this article had a chance to see the work of OSCE representatives in Luhansk Oblast half a year ago and now. It has changed considerably. Ukrainian military and officials admit that too.

On a typical February night six months ago, at the end of poorly lit street almost on the outskirts of Severodonetsk stands the brightly lit Myr hotel. Up to two dozen snow-dusted OSCE vehicles stand behind open gates.

"This is where the OSCE representatives live. Actually, I haven't seen them drive around our area. Maybe they are working in other zones," says a taxi driver that has brought me to the relatively peaceful Severodonetsk from the frontline in Novoaydar county a hundred kilometers away. We hear artillery shots somewhere on the outskirts of the city and wince involuntarily from the strong reverberations. The worries are over as soon as you enter the hotel. The sound does not go through the thick walls, so it is relatively comfortable to stay in it.

The hotel lobby is empty. Only the administrator is struggling to stay awake at the reception desk. We ask for free rooms and move in. In the evening guests come in, mainly foreigners with name tags. They sit down on large couches, chat about life, some get an update on the news on their laptops. The towns of Shchastya and Stanytsia Luhanska are being shelled at the moment. A pocket may soon appear near Debaltseve, a town in the adjacent Donetsk Oblast. The waitress brings beer. The guests from the EU stay there for an hour or two, pay the bill and disappear into the corridors.

"OSCE mission? They stay at the hotel more often than they work," Hennadiy Moskal, then Head of Luhansk Oblast State Administration, now transferred to the same position in Zakarpattia Oblast, used to lament. "Instead of going to the frontline, establishing violations and shelling, they spend days drinking and riding around the town in a taxi."

The next morning new people show up at the hotel restaurant. They, too, wear familiar name badges and carry laptops. The monitors sit down for breakfast, watch news, some type something in a Word document. They do not talk to strangers and smile to the waiters. The white OSCE car is still parked in

the hotel yard. Once breakfast is over, foreign guests head to their rooms.

Even during the day the restaurant is not empty. In its cozy room several monitors sip their coffee and beer with cordon bleu-like cutlets and healthy vegetable salads. More people visit the restaurant in the evening. They come in with their laptops and sit at the table to discuss the day. Some type texts or reports, while others order room service.

Closer to midnight one can hear the engines of cars roaring. A taxi pulls into a parking lot and several foreigners, men and women aged around 30, get out of the taxi. A young lad starts singing some pop song under the moonlight. Self-propelled artillery systems are shooting on the background. While foreign observers head to the administrator to get the keys, the roar of the artillery grows.

"OSCE? Observers?" an Aidar fighter Maestro laughs into the telephone. He is responsible for communication with the media in Shchastya. "No, they have not made it here. The shelling is so intense right now that a decision was taken to shut down town entrances and exits. This is the second day. But if you want, we can organize access and you can pass through the checkpoints. We can meet you, you can check out the damage. But this is at your own risk. The responsibility is on your shoulders."

Half a year ago the OSCE observers were not seen in the town of Shchastya, though it was presumed that they should have been there. Contrary to the agreements in Minsk, the separatists continued the war with Ukrainian armed forces. As a result, not only soldiers but civilians were dying. Over five days of our stay at the Myr hotel, we didn't see the mission go into the field even once.

In the summer of 2015 Myr has no vacant rooms. The administrator apologizes, says that all rooms are booked for the time being and recommends checking out other hotels. Just as half a year ago the white OSCE cars are parked outside. Two foreigners with sweets in plastic bags are walking towards the hotel. The two men enter the glass doors and disappear up the stairs. At around 9 p.m. observers traditionally gather on the couches in the restaurant and speak about life while slowly sipping on their red wine. A man orders cognac by the bar and speaks with the barman in accented Russian with the barman.

"The OSCE guys have started working. I saw their vehicles driving through our oblast," a local taxi driver claims. "They're not often in Severodonetsk as they mainly drive through the area. Of course, they use our local taxis. But they also go to the frontline."

"Whatever you say, the OSCE works more effectively this summer," says Ruslan Tkachuk, ATO spokesperson in Luhansk Oblast. "I believe this is due to rotation. They now have people with experience in conflict zones. I know a few of them. They have military schooling obtained in Great Britain. They are decisive and strong leaders that can consult their subordinates about how to behave on checkpoints and how to communicate with soldiers. The mission monitors are gradually establishing contacts with the military. The attitudes of soldiers towards the OSCE are gradually changing too. In the winter they could hardly stand OSCE monitors. Either they did not wave them through checkpoints or they simply stopped them.

Now, dialog takes place and the military are giving the monitors their contacts."

"Who heads the mission group is of great importance. People who have seen reactive artillery and mortar shelling before react to small arms more calmly and are not afraid to work in such circumstances," Ruslan says. "Then again, a lady comes from Paris, looks at us with her beautiful eyes, and we realize how distant she is from war. In general, the OSCE only sticks to its protocol. The monitors assume that all sides stick to it too. As a result, they sometimes get under shelling."

We arrive at Triokhizbenka. The familiar white jeeps are parked on the central square. Local residents are explaining something to two female monitors standing next to the jeeps.

"We have funny episodes. A feminist once came from Denmark to Ukraine to monitor the war. She does not understand the essence of the conflict and tries to convince people that the military actions are caused by gender inequality," Ruslan smiles. Monitors set to return to the hotel. Close to the night shelling is more likely.

"There was another story. OSCE Secretary visited us from Kyiv. The plans were to pay a visit to Triokhizbenka, but due to the military actions and the danger they decided to visit the more peaceful town of Shchastya, where they ended up under a line of fire. In Shchastya the OSCE representatives were to meet with their colleagues that were working on the territory controlled by

**"THE OSCE WORKS MORE EFFECTIVELY
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the Luhansk National Republic. As a result, two groups of monitors registered the violations of the Minsk agreements by the separatists. Even Russia was forced to admit this fact," Ruslan reported. Like OSCE monitors, we head to Severodonetsk.

"There are very few Russians among them. Most are British, Danes and French. There are also Ukrainians. Some of the foreigners speak quite good Russian," a soldier named Roman adds.

"The monitors are currently facing certain problems. They want to monitor the so-called grey zones. At least they expressed such a desire. However, getting there is rather difficult and this is a dilemma for the military forces because if they let in observers and shelling starts, somebody will get hurt, and that's the responsibility of the military. So, alternatives must be found. For example, there is the village Lobacheve. It is constantly under fire. I can go there to see how dangerous it is and what the local residents need. Then I return and tell the monitors everything I've seen," Ruslan adds.

Monitors relaxing in the local restaurants are far more rare than half a year ago. Foreigners spend most of their free time at the hotel.

"If you want to see OSCE monitors, check out the restaurant at Myr. That's where they usually take a rest in the evenings. Not all of them are suddenly working as one. Get patient and you'll run into some drunk observers riding around the town in a taxi. But that is getting more rare," Roman concludes. ■

An Unlikely Blend

Roman Malko

The origin and transformations of the Right Sector through the Maidan and war

Two years ago one could hardly speak of any serious influence of nationalists in Ukraine. Organizations of the kind have always been plenty here, but the system tried to sideline them or get them under control by weakening and dividing them. Nationalists themselves often played into the system's hands by getting into petty squabbles with each other, falling for provocation and turning into someone's puppets.

As soon as any patriotic movement with a radical ideology began gaining strength, a host of moles appeared in it, persecutions against its members started, its reputation was ruined by provocations, attempts of bribery or simply labels such as “fascists”, “Nazis”, “xenophobes”, etc. Security bureaus had departments that were responsible for such work. The most proactive members of nationalistic movements were regularly summoned to interviews with responsible agents.

This trend lasted through the entire period of Ukraine's independence. Control was occasionally weakened, then strengthened again, but it never disappeared.

BIRTH OF THE RIGHT SECTOR

Initially, the Right Sector was a union of different nationalistic civil and political organizations, which stood against the dictatorship of ex-president Viktor Yanukovich and the Party of Regions on the Maidan. Over time it transformed into a military-political movement officially known as Pravyi Sektor (Right Sector) party and Dobrovolchyi Ukrayinskiy Korpus (DUK, Voluntary Ukrainian Corpse), its paramilitary wing involved in the Anti-Terrorist Operation in Eastern Ukraine.

The Right Sector stems from the first days of the student camp protest on Maidan Nezalezhnosti, the Independence Square. Its founders were reportedly Andriy Kozubchuk who was killed in action near Donetsk airport in August 2014, and Mykola Surzhenko, the leader of the Sumy Ukrainian National Self-Defense (UNSO) nationalist organization. They proposed to turn the nationalist wing formed sporadically from some protesters into a separate group.

Initially, the Right Sector was based by the monument of the founders of Kyiv on Independence Square. Representatives of the Tryzub organization, UNSO and Patriots of Ukraine negotiated mutual actions and on November 28 the banner of the Right Sector was seen for the first time written in spray paint on a bed sheet. It was then joined by Carpathian Sich, a Zakarpattia-based paramilitary organization. It had long cooperated with Tryzub. Bilyi Molot (White Hammer, a small nationalist group of Kyiv-based skinheads) joined at some point as well.

WHO CREATED IT?

Apparently, the founders of the Right Sector officially included Tryzub, UNSO and Patriots of Ukraine that eventually transformed into the Social-National As-

sembly; Carpathian Sich and White Hammer. The first three are the most widely known so we will take a look at their background.

Ukrainian National Assembly – Ukrainian National Self-Defense (UNA-UNSO) was founded on November 3-4, 1990. It was involved in guarding the parliament of Lithuania during the January events in Vilnius in 1991, the “Friendship Train” to scare off separatists in early February 1992 in Odesa, Kherson and Crimea, the wars in Prydnistrovia and Abkhazia, the First Chechen War and other numerous events in Ukraine and beyond its borders. 1994 was its most active period. The second surge was during the violent clash between the police and participants of the funeral procession for St. Volodymyr, the Patriarch of the Ukrainian Orthodox Church of Kyiv Patriarchate, on Sofiyska Ploshcha in downtown Kyiv on July 18, 1995 – the day went into the history books as “Black Tuesday”. Yet another resonant act involving UNSO members happened on March 9, 2001 during the “Ukraine Without Kuchma” demonstration. It ended in a major scuffle with the police on Bankova Street. After this event several



THE FOUNDERS OF THE RIGHT SECTOR OFFICIALLY INCLUDED TRYZUB, UNSO, PATRIOTS OF UKRAINE, CARPATHIAN SICH AND WHITE HAMMER

UNSO activists were arrested and convicted. The organization then went into a series of crises and splits.

Tryzub is a paramilitary nationalist organization founded on October 14, 1993 and was registered as a Civil Sports-Patriotic Organization. The initiative was offered by Slava Stetsko, the then leader of the Organization of Ukrainian Nationalists (Revolutionaries). The greatest persecution of its members was in 1996-1998, when criminal proceedings were launched against its members all over Ukraine and then in 2010-2011 under the regime of Viktor Yanukovich when the members of Tryzub organized the demolition of the monument of Joseph Stalin in Zaporizhzhia.

The then government decided to exploit this to undermine the organization. An explosion of the monument was arranged and all of the organization's leaders were arrested under the pretext. They were accused of as much as plotting a terrorist attack on Yanukovich by shooting his plane from a low-caliber rifle. Given how ridiculous the charges looked, the case was quickly stifled.

The Patriots of Ukraine was founded in the late 1999 as a young wing of the Social-National Party of Ukraine, which later was renamed Svoboda. The predecessor to Patriots of Ukraine was Units of the Socio-Nationalist Party of Ukraine. In 2004, Patriots of Ukraine was disbanded



The peak of UNA-UNSO: A clash with the police at the Ukraine Without Kuchma rally on March 9, 2001

due to internal party conflicts, but then it was revived in Kharkiv and later in Kyiv.

After that its hubs began quickly appearing in the majority of cities across Ukraine. In 2008 the organization was a co-founder of the Socio-National Assembly comprised of Patriots of Ukraine, the RiD national movement, the Ukrainian Alternative and Sich. In the summer of 2011, the organization faced a series of persecutions and arrests of many of its leaders, primarily for fabricated charges. Some were charged with organization of terrorist acts and others were suspected of assassination. They were only released from jail after the Maidan.

FURTHER TRANSFORMATIONS

The beating of students on the night of November 30 was the first test of sorts for the Right Sector. The few activists then tried to stave off the offensive of the Berkut riot police, but it was impossible as the latter were stronger in force. On the following day, when the center of the protest moved to the Mykhailivsky Monastery and square, and the police began to move there, the future Right Sector started forming self-defense units and training them. Ostensibly, Dmytro Korchynskiy tried to join the movement with his Bratstvo (Brotherhood) organization, but cooperation failed. Apparently, Korchynskiy already then offered to dig out and prepare street cobbles but most Right Sector members refused to do that. The Right Sector admits that at the time it was not ready for this. "He proposed that which transpired within a month, but in history everything has its proper moment."

During the rally on Bankova St. on December 1 many Right Sector members took part and some even seized the building of the Kyiv City State Administration but vacated it later as they did not want to provoke average citizens who started to seize activists and hand them over to the police. It turned into a more or less complete structure only after it settled on the fifth floor of the Trade Unions' Building.

On the day before Epiphany on January 18 members of the Right Sector – i.e. members of Tryzub and UNSO – were invited to a meeting with the inner circle of Vitaliy Klitschko where a plan of activation and possible march of demonstrators to the parliament was ostensibly being developed. The plan was reportedly ready and waiting for



Contemporary Banderites: Members of the Stepan Bandera Tryzub organization making its 20th anniversary

a green light from the leadership. In the evening of January 18 Klitschko reversed the plan and informed the protesters through his representatives that the march would not happen. On January 19, someone from AutoMaidan called on the protesters to start moving towards the Verkhovna Rada. Weary of uncertainty, people started moving closer to the police cordons. The Right Sector divisions moved to their positions as well. Self-Defense units were already there, and a number of small clashes with the police broke out. Klitschko, in an attempt to calm down the crowd, got sprayed with the fire extinguisher and a series clash broke out. That one involved the Right Sector, Self-Defense and simply unknown people.

Today, the Right Sector is not so much a union organized by founders as it is a structure created on the basis of Tryzub and UNSO. The movement has welcomed anyone who wanted to join it, whether members of patriotic movements or not. The Right Sector party entered politics after renaming UNSO's political wing, the Ukrainian National Assembly. Notably, Patriot of Ukraine, Carpathian Sich or the White Hammer have no relation to it today.

At the initial stage, the Patriot of Ukraine within the Right Sector was delegated the mission of working in Eastern Ukraine under the leadership of Andriy Biletskyi and Oleh Odnorozhenko. This scheme did not work and they went their separate ways by forming Azov battalion. Carpathian Sich also split away.

Although many UNSO members, primarily of the older generation, hold top positions in the Right Sector, a small faction of UNSO has recently split away and re-registered the organization. Cooperation with the White Hammer failed from the very beginning. The skinheads turned out to be uncontrollable and, witnesses claim, they were split off from the Right Sector right after the end of the Maidan.

Since the Maidan the structure of the Private Sector has changed considerably. Many of its members who had volunteered to fight in the East joined different battalions and units of the Armed Forces of Ukraine as negotiations on the setup of DUK with the central government dragged on. Yet, they remain members of the Right Sector.

Its leaders don't see this as a problem. There is no obligation for the Right Sector members to fight in DUK exclusively. ■



PHOTO BY UNIAN

Andriy Stempitsky:

“The state machine is working to discredit us”

Interview by
**Roman
Malko**

Commander of the Ukrainian Volunteer Corps, a paramilitary unit of the Right Sector, spoke to *The Ukrainian Week* about risks in the Minsk accords, the pressure of Ukraine's on the Right Sector, and things to be done to win the war.

How have your relations with the government changed after the incident in Mukacheve?

There has been increasing pressure on reserve battalions. Commanders report about the morbid interest of law enforcement and security agencies in the numbers, bases, locations, lists of those fighting on the front line, etc. In Zakarpattia, both the reserve battalion and the Right Sector overall are facing huge pressure. I have heard today from Volyn Oblast: the number of call-up papers precisely coincides with the number of the Right Sector members. If five of our members reside in a certain county, five call-ups for mobilization go there. This is done intentionally. For some reason, they think that our men shun mobilization or military service. But this is not the problem, because many have been at the front for more than a year now. This is an attempt to disperse active members across military units and isolate them in this way.

Has the incident undermined your positions in Zakarpattia?

Zakarpattia is a multi-ethnic region, and not everyone there was happy with the Right Sector before. But after the events in Mukachevo the support for the Right Sector among the population has grown immensely. This is a fact. Yes, shots were fired, even mortars were used, it is a shame that it happened so far from the front line. But in that situation our men had no other way out, they were virtually being wiped out, and for some reason they did not feel like dying. They were under fire from a large calibre machine gun, one in a car was already shot dead, and they opened mortar fire in response. The shooting stopped, and they were able to retreat to the mountains. Many accuse them of opening fire in the middle of a peaceful town, with civilians and children around. This is not how it really happened. The scene was outside the town, on the bypass, and it is the police responsible for the operation, that should answer why fire was opened exactly on that spot. Our men definitely had no intention or desire to fight with the police. They were on their way to negotiate with the bandits who had threatened them and their families. Their message to us was clear: either you forget about blocking the contraband, or we will deal with you, your families in-

cluded, in a totally different manner. So the guys went to dot the i's and cross the t's, and they hoped to handle that without shooting, but they knew perfectly well who they were dealing with and where they were going, and that those local gangsters have plenty of weapons. For some reason, this is somehow hushed up. And most interestingly, after the shooting no one was detained from the other party. Theoretically, everything should be fair. Our guys had guns, those guys had guns, too. There were searches, but not a single arrest. Which means that the other party may shoot, may carry guns, but if the Right Sector does the same, it qualifies as a terrorist attack. Like recently in Rivne Oblast, at the illegal amber mines - there were mass riots and shootings, but it is okay because the Right Sector was not involved. If we had been, the incident would have been labelled as mass terrorism.

Do you cooperate in this case with the new governor of Zakarpattia, Hennadiy Moskal? Do you trust him?

No, we haven't, and we don't now. He had a negative attitude towards the Right Sector back in Luhansk Oblast, although we did not participate in hostilities there. And when he came to Zakarpattia, he immediately made a statement about 80% Right Sector members with a criminal record, calling up women to the army, and so on. It is quite obvious what his goal here is, and how he is going to handle the Right Sector in Zakarpattia.

According to the Right Sector, it has two units on the front line, while in the rear there are nearly two dozen. Why so many? What are they doing, what is their mission in the rear?

Reserve battalions are meant for the people who wish to fight as members of the Right Sector's Ukrainian Volunteer Corps (known by the abbreviation of DUK in Ukrainian — **Ed.**), so that they know where they can come and enlist. Some have training bases, where you can get schooling, and not only for the front. The battalions have other missions in the rear as well, such as supply and delivery. Our men are trying to provide the fighting battalions and support those coming back from the front, so that they do not get lost in the whirlpool of life, but stay in the ranks of the organization.

Will the government attempt complete clampdown on the Right Sector?

I think this is what it has been busy doing. The only things that do change are intensity and methods. The clampdown of the Right Sector does not have necessarily to be physical: encircled, assaulted, and disarmed. It also involves discrediting.

Sometimes they are trying to throw volunteers behind the bars, sometimes they are trying to throw the book at them. No one says that our units are comprised of angels alone; of course, they are real people, and different at that. But the trend is obvious, even in case with other battalions. Take Battalion Tornado, how it was discredited and destroyed, or certain events within Aidar. The government has tested its methods, and is trying to apply those methods to us.

How are you going to counter the recently launched "de-heroization" campaign? Some are now saying that you did not fight at the Donetsk Airport, or that you were never present in other locations. Is there a way to counter it?

We probably haven't been on the Maidan either. We joked back then that a time would come when some would say that we had never been there. We hear this now. Then a time will come when they will say we never fought in this war. For example, our men resent Yuriy Biriukov's (volunteer who was eventually appointed advisor to the President and aide to the Defense Minister mostly responsible for supplies for the military — **Ed.**) words the most, who said that we fled the airport. It is the army command that asked us to withdraw. And back then we said that as soon as we withdrew, the airport would be surrendered. Likewise, the same will be later said of Shyrokyne or other places from which we withdrew. Our men hate retreats by definition. And if such things happened, they happened in coordination with the Armed Forces. We always hear the same tune: you are volunteers, you must cooperate, discipline above all. And later this is used against us.

Of course, we counter it in every possible way. Our counter-intelligence on the front line is also in charge of internal security. There also is the Right Sector security service, which tries to work preventively.

You propose to legalize the Ukrainian Volunteer Corps along the Estonian or Swiss model. At any rate, this involves legalization of weapons. Is this government prepared to let people carry firearms?

This government, just like all the predecessors, is not prepared to let people carry firearms, because an armed civilian is a free man, even if psychologically. And who needs free people here? No one, because they are not so easy to handle. Especially in the way our government does.

On the other hand, our proposed bill does not state that weapons should be handed out immediately, as the Estonian version does. In Estonia everything is put very clearly: individuals may have up to seven or nine firearms in the house, and they undergo training. At any giv-

"OUR MEN IN RESERVE BATTALIONS ARE TRYING TO PROVIDE THE FIGHTING BATTALIONS AND SUPPORT THOSE COMING BACK FROM THE FRONT"

en moment they can be mobilized, rebuff an enemy attack, or deal with other challenges. We have proposed a moderate variant of the bill: there are reserve battalions, and if a situation arises in the country and their help is needed, they become subordinated to the structure charged with handling the challenge. We do not strive to replace any of the power-wielding structures: the Armed Forces, the Ministry of the Interior, or the Security Bureau of Ukraine (SBU). They have their own objectives defined by the Constitution: the Armed Forces to repulse exterior aggression, the Ministry of Interior to deal with domestic problems, the SBU to watch over state security. Under the proposed legislation, we would like to be an auxiliary structure. If there is an anti-terrorist operation going on, the reserve battalions could be used (under the SBU supervision) to form battle units, which would be subordinate to the commander of the Anti-Terrorist Centre. There they would receive weapons and supplies, complete their objective and go back to their respective battalions. In case of external aggression, war, battle »

units would be formed according to the orders of the Commander-in-Chief and subsequently subordinated to the Chief of Staff.

To what extent is DUK dependent on the Right Sector Party, how far does your independence stretch? Are you interested in the party membership for all of your fighters?

The Right Sector is a nationwide movement. It arose on Maidan as a certain, unique phenomenon. It was not a political party or a military unit. It was exactly a movement, active, capable, comprising active young men and women, both organized and unorganized. Later, after the Maidan events, in the new situation a part of people crystallized who were ready to face Russia's challenge, because then the events in Crimea and in the East began. Thus, two wings appeared, the political and the military one. Like the right and left arms. Each has its own objectives, and DUK cannot be dependent on the party, just like the party cannot depend on DUK. In brief, the Right Sector has political objectives, whereas DUK fighters have military objectives, first and foremost, fighting the occupants who invaded our country. But all of them are united by one idea: creating of a normal, strong Ukrainian state. The political party declares this in its programme, in its propaganda materials, explains this at meetings with people, while DUK fighters make their declaration on the front line.

What kind of relations do you have with the military?

We have extremely cordial, brotherly relations with the soldiers who are fighting now and who fought last year. In the trenches there is no difference between volunteers and regular army men, nor does the enemy make any difference between the former and the latter. There are joint battle missions, normal cooperation with commanders and soldiers. The problem lies elsewhere: a lot of fighters in last year's operations are now demobbed, and new men are called up, and they got to hear how bad the Right Sector is, how it evades fighting and engages in all sorts of illegal activities — and some of those men believe this nonsense. Well, at least until they meet our guys and realize that it is not true. But the state machine is working to discredit us, even in the Armed Forces.

Volunteers are often accused of marauding. How widespread is this evil, is it present in DUK, and how do you prevent it?

It is easier for us to counter it because we have a totally different motivation level, and such things happen on a much smaller scale. For instance, if in the regular army drinking is punished by confinement in the guardhouse or otherwise, our worst punishment is banishment from the front line or even expulsion from DUK. Just the opposite: we punish someone so that they cannot fight anymore. All sorts of things happen, like drinking or unworthy conduct, and such individuals are expelled from our system. Most commanders have gained enough experience to be able to foresee each individual's propensities, and if they do not fit the frames, such individual is dismissed. This is how we fight negative tendencies. Prevention comes first, and moreover, we do not limit ourselves to some certain methods of punishment. There are various ways to influence an individual and make them loath to commit a crime, and this is quite normal.

Andrii Stempitsky is the commander in chief of the Stepan Bandera Nationwide Organisation Tryzub (Trident), deputy leader of the Right Sector, commandant of DUK. Born in Lviv Oblast, Stempitsky studied to become a pilot/navigator at the Higher Air Force School in Kharkiv. He is an active member of the national liberation movement, member of the Stepan Bandera NO Tryzub since 1995. In 1996 Stempitsky was convicted (for a five-year term) for participation in an attempt to seize a military airfield. He has been acting commander in chief of Tryzub after October 2010, becoming commander in chief in October 2012

Your organisation is criticised for large numbers of fighters with a criminal record. Current Zakarpattia Governor Moskal mentioned 80% of such people within the Right Sector in the oblast. How large is the actual share?

Moskal went too far. 80% fighters with a criminal record is ridiculous. The Right Sector in Zakarpattia consists of several companies of young men and women. They are normal people who have been conducting extensive political activities, worked with the youth and children. This is proven by video materials, there is enough evidence on our web-sites, anywhere. All year long no comments had been made, until Moskal's statement out of the blue.

Of course, among DUK fighters there will be people with a criminal record, and maybe among the Right Sector as well. A small percentage. But firstly, when such people enlist in DUK in order to go to the front, they go through a screening. The character of their conviction is checked. If someone was convicted for rape or some pathological theft, he has no place among us: a leopard cannot change its spots. If they were convicted for murder for profit or have any sadistic proclivity, they do not belong in DUK either. But if it was a petty offence, why should a person be deprived of the right to fight for their Fatherland? We have had too many law-abiding, crystal-clear prosecutors, police officers, security service agents, who defected to Russia en masse. They had no record, they enforced and represented the law. So in my opinion, it is not the matter of criminal record, it is the matter of personality. Many men with a record have proved to be worthy in battle and would leave many of those clean ones in the dust. By the by, I have two convictions, too.

On political grounds?

They were classified as criminal. The main thing is to get an insight into the newcomer's motivation. Once that is clear, it is easy to see if we belong together or not.

Russia is closely following the Right Sector and its activities. There have most probably been attempts to infiltrate FSB agents in your organisation. Have you ever unmasked any of them? Speaking of your counter-intelligence and Right Sector security service which you have mentioned above: could you share more about their activities?

I will not go into the details. Even the "Donetsk People's Republic" agents have been revealed. Sometimes destructive individuals infiltrate, and then the security service tracks down the chain: who they are, who profits from it, and so on. Methods of their subversive activities can vary. Some are saboteurs, others spread rumours or spread panic, but we cope with that. Like I told, we have counter-intelligence which deals with battle units, and the security service which is active in the rear. Each of them screen and processes the data to see what kind of person wants to join the organisation, and what their

sentiments and intentions are. Some may have material motives and want to profit exploiting the name of the Right Sector, others seek to make a petty political career at all costs, still others come here just by accident. The services work on it and recommend the commanders or political structures to expel such individuals or restrict their activities.

What do you do with prisoners? Do you torture or swap them?

We have not had that many prisoners. Torture is forbidden here. This is no place to realize one's sadistic proclivities. Consequently, whatever PoWs we had, were exchanged.

Did you do that personally?

Yes. To establish contacts and organise exchange is not so easy, but it is doable. When we come across some fishy subjects, we hand them over to the SBU, which has to decide what to do with them further. One example is Serhiy Sazhko, mayor of Kurakhove. He has organised referendums, was engaged in pro-DPR propaganda among the population, the agencies have his video- and written testimony (which he made without any physical coercion) — all of this was handed over to the SBU. Nevertheless, he managed to become a member of parliament. This shows the efficiency of the state in fighting separatists. But this does not mean that the SBU or counter-intelligence are not doing their work: they are just dependent on the laws they enforce. They are restricted by these laws in their activities. Peacetime legislation is imperfect, and Russia has unleashed a war against us. Yet judging from what is going on in the country, one has an impression that there is no war whatsoever. Hence this imbalance. The other side does what it will, missing no opportunity to promote its evil cause, and on this side they cannot offer decent counter-action because it is illegal.

What are your losses in this war?

Until recently, we had 35 people killed, and now that fighting has resumed that will be 39 or 40. We have several hundred wounded, taking into consideration all degrees, from light to medium to gravely injured. With those who were temporarily disabled, I think the casualties will add up to at least two hundred.

How do you help the maimed members and the families of the deceased?

We have our own medical service, Hospitalers, led by Yana Zinkevych. The service is organized everywhere where our units engage in hostilities. There are medical crews who give first aid not only to our fighters, but also to those of other voluntary battalions. Medics recover the wounded under fire, deliver them to the nearest hospitals and later, when their condition is stabilised, transport them to the Mechnikov Clinic in Dnipropetrovsk, where the wounded get specialist care. Their professionalism helped save very many lives.

The medical service also takes care of the wounded. If additional help is needed, or in case of emergency, we raise funds (again, with the help of Ukrainians who donate and transfer money), etc. If someone wants to take a family under their patronage, we help to establish direct contact, so that we do not act as an intermediary. We also look for possibilities to organise holidays for chil-

dren. There are people who are willing to help. That is, we do everything we can. The reserve battalions, too, are charged with taking care of the families of the deceased and wounded. Because oblivion is the worst that can happen to their children and families.

You demands include cancellation of the Minsk accords and a war till victory is won. Is the Ukrainian army capable of fighting successfully and win back the occupied territories of Donbas and Crimea?

Yes, we insist on the abolishment of the Minsk accords, because what are they, as a matter of fact? Firstly, a simple question: who is negotiating with the terrorists? Medvedchuk, Kuchma, and other 'statesmen.' Who actually authorised them to negotiate? Did the Verkhovna Rada or President do? Secondly, the very idea of negotiating with terrorists seems somewhat wrong. No country ever conducts any talks with terrorists. Moreover, the fulfilment of the Minsk accords could be considered criminal offense just a couple of years later. That is, those officers and soldiers who withhold reprisal fire today, while they are being shot at, might find themselves in the dock a couple of years later. Will they be telling about the Minsk accords then? What accords are these, who was the negotiator, and so on, and so forth?

Besides, the Russian army is said to be more powerful than that of Ukraine. That's true, they certainly have a lot more guns and vehicles, and there is no lack of cannon fodder either. But then there are several aspects to consider. Firstly, Ukrainians wage a defensive war, they

"IF THERE IS AN ANTI-TERRORIST OPERATION GOING ON, OUR RESERVE BATTALIONS COULD BE USED UNDER THE SBU SUPERVISION TO FORM BATTLE UNITS SUBORDINATE TO THE COMMANDER OF THE ANTI-TERRORIST CENTRE"

defend their land while Russians are occupiers and, of course, both parties have different motivation. It is easier to die for your own family and Fatherland than for some obscure goals, invading a strange country. Secondly, the tactics of warfare. If the enemy prevails in force, different tactics should be employed. This is clear. We cannot compete with them according to the books dating back to 1942, engaging in trench warfare and building some defence barriers and squandering millions to no avail. Modern war is dynamic, mobile, just as those barriers are. What we have now resembles the First World War, when opponents sat in trenches for years banging cannonballs at each other. This is nothing but mindless waste of money which should actually be used to develop drones and other new technologies.

How could this stalemate be broken?

Pressure on the government can change everything. We have witnessed it in 2013: no matter what the pessimists say, it turns out that the people can do a lot. But we have a problem: there is potential, but no mechanism to implement it. The parties have carved up the society. Each is trying to win over the electorate, and there is no powerful unity of all Ukrainians to solve all problems at one fell swoop. Divide and rule. ■

Yet Another Russia: On Andrei Piontkovsky

Leonidas Donskis

Very few political analysts and commentators possess the gift of the metaphor coupled with the incisiveness and accuracy of analysis. Either they fail a method or they fail a story, as Umberto Eco would have it. And yet there is a political analyst and writer who reconciles both the analytic skills and the powers of a graceful metaphor.

The name of the writer in question is Andrei Piontkovsky who celebrated his 75th birthday this summer. A brilliant polemicist, writer, and political analyst, Piontkovsky established himself as an irreconcilable antagonist of Vladimir Putin and Putinism. In doing so, he has coined such unforgettable and winged expressions as, for instance, “we are dust in the wind, and Putin is our President,” or “the treacherous Putin is cheating on Russia with the corpse of the Soviet Union.” Russia in his mercilessly caustic and analytic writings becomes an unloved country whose sad destiny lies in her being confined to the monster that is good only to scare the civilized world.

Yet Piontkovsky is far from hopelessness and fatalism. His polemical opinion pieces and political analyses are full of irony, wit, boldness, and courage. True, sometimes he sounds gloomy and sombre, but this does not last long. As soon as he detects and identifies the weaknesses of the regime, we can hear an energetic and strong voice of the unbreakable and deeply committed public intellectual who knows perfectly well that he cannot fail the right cause.

In the era of the former Soviet Union, Western journalists were frequently poking fun of Sovietologists, or Kremlinologists, as they were christened in those days. They seem to have had a good reason for this, as the vast majority of their premises and generalizations proved false and ridiculous. Nothing was astonishing in this, though. The self-contained world of Soviet politics coupled with suspicion, paranoia, and mistrust, called for a special art of deciphering the symbols of power and loyalty in the Kremlin. Those who stood closer to the deceased leader or those who were bidding farewell to him with exceptional solemnity used to be identified by Kremlinologists as legitimate and more or less obvious heirs to the Party's power and legacy.

Much to my astonishment, things are as close to this sort of modern black magic now as they were in those Soviet days. We can only wonder at the futility of the predictions of the outcome or at least of further dynamics of the war in Ukraine and the resulting crisis in the relations between the West and Russia. On the one side, this indicates the flashback: Russian politics has become as hermetical and unpredictable as was in those old days with the former USSR; on the other side, it tells something disturbing about the most unpleasant tendencies of present journalism, one of which is the industry of fear.



Repeating a thousand times a day that the West is weak and Vladimir Putin is strong, or that the EU is just about to collapse due the bankruptcy of Greece, or that Ukraine's demise is imminent, exposes commentators' own fears and disbelief in our ability to defend our liberal values and democratic politics. Not only does it distort reality; it paves the way for scaremongering and defeatism – things that do not help us to find a way out of present political tensions, economic predicaments, and moral dilemmas.

Therefore, we have to be trained to panic, according to the logic of scaremongering. Be scared more than the others to be able to shape the public opinion. As Günther Anders wrote in 1960: “Don't be scared to be afraid, have the courage to be afraid. And have the courage to scare others. Communicate to your neighbours a fear at least as great as your own”.

REPEATING A THOUSAND TIMES A DAY THAT THE WEST IS WEAK AND VLADIMIR PUTIN IS STRONG EXPOSES COMMENTATORS' OWN FEARS AND DISBELIEF IN OUR ABILITY TO DEFEND OUR LIBERAL VALUES

This phenomenon seems deeply embedded in what Pascal Bruckner termed the fanaticism of the apocalypse.

None of these could be found in Andrei Piontkovsky's political analyses and commentaries – instead, he appears as the one who tries to win back our threatened sense of self-confidence and sober-mindedness. If I could come up with the best candidate for the award for intellectual courage, analytic brilliance, moderate optimism, and hope, I would certainly opt for Piontkovsky. If my country, Lithuania, was able to resist and not to succumb to mass psychosis, fear, and panic during Russia's nuclear blackmail and other provocations, it was due to such writers as him.

Even Andrei Piontkovsky, no matter how insightful and bright, may not know one thing – namely, that we are at the peril of finding ourselves neither on the winning nor on the losing side in our battle against Putinism. Putin and his grotesque regime are inexorably doomed, yet the cost of his defeat may well be our curse to live neither in war nor in peace. This sort of low-intensity conflicts and tensions create the unprecedented level of uncertainty even in those cases when the truth, legitimacy, and hard-won success is on our side.

Therefore, we should be deeply grateful to Andrei Piontkovsky not only for reminding us of yet another Russia with her such defenders of freedom and human dignity as himself, but also for his fearlessness and optimism – the traits that our troubled world needs the most. ■



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PLAN BIG



MEET BIG



REWARD BIG

BENEFIT WHEN BOOKING AN EVENT WITH HILTON KYIV

events with total budget over 7500 EUR are entitled to select two options from the list:

- 5% of the total amount as a credit for the next event
- One complimentary welcome coffee break (coffee/tea, cookies)
- One complimentary guest room per every 20 rooms booked (maximum of two complimentary rooms per group)
- One complimentary upgrade to Deluxe guest room per every 10 rooms booked
- One complimentary room cancellation on the day of arrival
- 5% off on audio/visual rental equipment
- 200 UAH spa credit per delegate to be used during the group stay (not applicable on spa products, merchandise and Thai massage)
- Gift voucher for a weekend stay
- Gift voucher to spa day use